Submission

by the

Government of the Province of Alberta

Concerning the

Report of the Royal Commission on Taxation

December 1967

PROVINCIAL TREASURER

ALBERTA

December 29, 1967.

The Honourable Mitchell F. Sharp,
Minister of Finance,
Government of Canada,
OTTAWA, Ontario.

Dear Mr. Sharp:

The attached brief presents the results of a comprehensive study undertaken by the Government of Alberta concerning the Report of the Royal Commission on Taxation. This brief is respectfully submitted in response to your request for comments on certain recommendations made by the Commission.

An understanding of the importance of certain natural resources to the economic growth of Alberta is necessary in order to properly assess the impact which many Commission recommendations would have on the future development of our Province. This subject is discussed in Chapter II of our brief.

Chapter III outlines ways in which rapid economic development of Alberta has been of benefit to all of Canada.

The specific impacts of implementation of certain Commission recommendations on agriculture, the petroleum industry and the Government of Alberta are discussed in Chapters IV, V and VI, respectively.

Chapter VII includes a review of apparent Commission philosophy and certain major recommendations. In order to clearly illustrate differences between stated policy of the Government of Alberta and concepts and philosophy proposed by the Commission, frequent reference is made throughout Chapter VII to the White Paper on Human Resources Development which was released in March 1967 by the Government of Alberta.

A concise summary of our brief is contained in Chapter I immediately following this letter of transmittal.

While the Government of Alberta opposes the implementation of a number of the major recommendations of the Royal Commission on Taxation this does not mean we are against appropriate tax reform.

Yours sincerely,

Anders Aalborg

ANDERS O. AALBORG.

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Chapter I

SUMMARY

The Importance of Natural Resources To The Economic Development of Alberta (See Chapter II)

Agriculture and mineral development are the major sectors of the Alberta economy. An understanding of their important contribution to economic growth is necessary in order to properly assess the adverse effect which implementation of certain recommendations of the Royal Commission on Taxation would have on future economic development of the Province.

Improved or unimproved farm land makes up about 30 per cent of Alberta's total land area and about 27 per cent of Canada's total farm area. Alberta raises approximately 30 per cent of Canada's total livestock population. Alberta farms also account for approximately 20 per cent of the total value of Canadian wheat production and higher proportions of total Canadian oats and barley production.

Alberta contains large reserves of a number of important minerals, including over 80 per cent of total Canadian reserves of crude oil and natural gas. Production of crude oil, natural gas and sulphur together account for 80 per cent to 90 per cent of the total value of Alberta's mineral production.

Agriculture and mineral production account for the major portion of Alberta's net value of general industry production.

Initially, economic development resulted from farming and ranching operations. Settlement in more remote areas continued until the 1929 Depression. Alberta's growth was minimal from 1929 until the outbreak of World War II. Discovery of crude oil at Leduc in 1947 resulted in relatively rapid growth and diversification of the Provincial economy during the past twenty years. Total cash expenditures for exploration, development and producing operations of the petroleum industry in Alberta currently approximate $750,000,000 per year. These sizeable annual expenditures have attracted many new businesses to Alberta. The total labour force has increased substantially since 1947 despite a significant drop in the size of the labour force employed in agriculture.

Direct payments by the petroleum industry to the Government of Alberta are in the order of 50 per cent of total net revenues of the Province.

The Importance of Alberta's Economic Development To Canada (See Chapter III)

Rapid economic development of Alberta since 1947 has been of major significance to the remainder of Canada in a number of ways, including:

1. Agriculture and petroleum industry activities have increased, more than proportionately, the demand for many products manufactured in Eastern Canada;

2. The movement of manufactured products to Alberta markets and movement of agricultural and mineral production from Alberta to domestic and export markets have been of great importance to the Canadian transportation industry;

3. Exports of grain and petroleum products have made an important contribution to Canada's international balance of trade. For example, in 1965 export of these commodities accounted for nearly 20 per cent of Canada's total export trade. A significant portion of these exports originated in Alberta.

4. Discovery and development of large crude oil and natural gas reserves provided Canada with an assured supply of these important forms of energy. At present, crude oil and natural gas supply over 70 per cent of total Canadian energy requirements. The uncertainty of long-run availability of certain foreign crude oil supplies owing to periodic interruption of production accentuates the need for maintaining large Canadian reserves and adequate producing and transportation facilities; and

5. despite a rapid increase in Alberta's population, gross payments to the Province by the Federal Government have decreased in relative importance, particularly since 1957.

Implementation of major recommendations of the Royal Commission on Taxation which would adversely affect the future economic development of Alberta obviously would have serious repercussions for Canada as a whole.

The Impact of Commission Recommendations on Farming and Ranching Operations (See Chapter IV)

The following Commission recommendations, if implemented, would create serious problems for farmers and ranchers:

1. conversion from a "cash" to an "accrual" method of calculating taxable income;

2. taxation of capital gains realized from the disposition of farm property; and

3. taxation of gifts and bequests.

An accrual basis for calculating tax would increase the immediate exposure of farm income to taxation and would complicate accounting procedures. For example, evaluation of livestock or grain inventory can be extremely complex. The fact that the cash method of accounting does not require inclusion of substantial inventories in income is considered a serious void by the Commission. Under the proposed accrual system, farmers could not defer tax payments on inventory until income is received. Serious hardships could develop in years of heavy inventory build-up resulting from a combination of low market demand and high crop yields.

Under the proposed accrual system, grain farmers would have a unique and unfair tax burden imposed upon them since accounts receivable would be included in the calculation of taxable income. Requiring farmers to bring accounts receivable into taxable income would be the equivalent of burdening them with annual interest payments since they would, in effect, be prepaying taxes on monies which would not be received for an extended period. The Commission did not appear to adequately consider grain delivery and payment procedures.

The proposed taxes on capital gains and bequests and gifts, would increase the tax exposure on any transfer of farm or ranch assets. The assets would be taxed in the following ways:

1. on capital gains realized by the estate; and

2. on the value of the estate (less taxes paid by the deceased) which would be brought into the beneficiary's income at full progressive rates.

This "double" taxation at full and progressive rates would likely precipitate the breaking up of farm units in order to provide funds to meet accrued taxes. The eventual outcome could be transfer of ownership of Canadian farms or ranches to large and probably non-resident investors. Quite apart from the very damaging effect this would have on individual incentive, is the fact that it completely contradicts sound economic principles. Farms must be of a certain minimum size in order to constitute an economic unit. The nature of farming and ranching operations in the Prairie Provinces requires much larger-sized units than are necessary in the remainder of Canada.

The Commission's failure to take into account the impact of inflation on land values also would have serious implications for farmers and ranchers. Taxation of capital gains on inflated land prices would create a financial hardship for families wishing to transfer land title to relatives outside the family unit or wishing to plan for their financial security upon retirement.

These examples reflect only a few ways in which the Commission's recommendations would adversely affect farming and ranching operations in Western Canada. Over 70 per cent of tax-paying farmers are located in Western Canada. They contribute 67 per cent of the national tax revenue from agriculture. Changes in tax legislation, which would adversely affect farming operations, therefore, would bear more heavily on the residents of Western Canada.

Our taxation system should be designed to encourage development of highly productive farming and ranching operations. In our opinion, implementation of taxation on capital gains, bequest and gifts, and changes in methods of determining taxable income would have the reverse effect.

<u>The Impact of Commission Recommendations on the Petroleum Industry (See Chapter V)</u>

The Commission's proposals for taxation of the extractive industries, particularly the removal of the depletion allowance and

change in write-off provisions, would reduce the level of exploration and development activities in the Canadian petroleum industry. A reduction of these activities would have serious implications for residents of Alberta and the Government of Alberta. In our opinion, the Commission ignored the serious impact of its recommendations, if implemented, on the long-range economic development of Alberta.

The Commission's analysis of the petroleum industry was based on certain erroneous assumptions and on unrealistic application of economic theories. The Commission showed a lack of understanding of the petroleum industry particularly in its assessment of the Athabasca Tar Sands.

The Commission's recommendations for eliminating depletion allowances and changing write-off provisions apparently were based on its interpretation of the present and near-future status of Tar Sands development.

The economic operation of a Tar Sands plant requires reasonably constant throughput at close to capacity which builds a degree of inflexibility into production. Conventional oil reserves offer flexibility to accommodate sudden increases in domestic or export demands.

Contrary to the Commission's belief, it has not been proven that Tar Sands crude is available in limitless quantities nor have methods of extracting oil in commercial quantities been subjected to the test of time. Development of the Great Canadian Oil Sands project, which only commenced production on September 30, 1967, depended on the existence of depletion allowance, the three-year exemption of mines from tax payment, and the timing of eligibility for capital cost allowances. It is surprising that the Commission stressed Tar Sands production yet, at the same time, recommended removal of the very same incentives which made the GCOS project viable.

The Commission overlooked the fact that marketable natural gas is not available from Tar Sands operations. Additions to natural gas reserves, therefore, are dependent on continuation of conventional exploration and development activities.

We are also concerned that the Commission:

1. did not attach sufficient importance to the risks and uncertainties prevalent in oil exploration and development;

2. did not give attention to long-range potential outlook for Canadian oil and gas production and to the unpredictability of exploration activities;

3. incorrectly concluded that removal of industry incentives would result in the diversion or allocation of international oil investment capital to other Canadian industries;

4. grossly underestimated the total burden of taxation of the petroleum industry by limiting its analysis only to government revenues received from corporation taxes paid by petroleum companies.

Also, we strongly object to the Commission's proposal that, as far as the extractive industries are concerned, subsidies would be preferable to present incentives.

Because the petroleum industry is so vital to the economy of Alberta, to the other provinces of Western Canada and to the remainder of Canada, we strongly recommend rejection of the Commission's recommendations for taxation of the extractive industries.

Implications of Commission Recommendations on Federal-Provincial Fiscal Relations and Alberta's Fiscal Capacity (See Chapter VI)

The Commission recommendation that the provinces (1) abandon corporate taxes and succession duties, (2) accept an upper limit on their share of personal income taxes, (3) accept integration of personal and corporate taxes, etcetera, would result in further centralization of fiscal control with the Federal Government.

The loss of provincial autonomy implicit in these recommendations would seriously impair the provincial governments' abilities to carry out their constitutional responsibilities. Provincial governments are more conversant with their respective regional needs and problems than federal agencies. Therefore, in order to properly perform their individual responsibilities, provincial governments must be assured of autonomy in their fields accompanied with adequate fiscal capacity.

The Province of Alberta is concerned that the Commission's proposal for provincial governments to withdraw from, or have restricted access to, certain sources of taxation would further impair its fiscal capacity. More than two-thirds of Alberta's estimated net revenue for the fiscal year ending March 31, 1968 would come from two major sources - direct revenues received from the petroleum industry and corporate and personal income taxes. Both would be affected by the Commission's recommendations.

Alberta Government revenues from the petroleum industry could be reduced by an estimated $40 million to $80 million in 1970, and by $75 million to $150 million by 1975 if Commission recommendations for taxation of the extractive industries are implemented. Reductions of such magnitude, which have been estimated on a conservative basis, are viewed with great concern by the Government of Alberta.

Further, loss of the corporate tax would mean the Government of Alberta would forego projected revenue amounting to $40 million in 1970 and $55 million in 1975.

The Commission's suggestion with respect to retail sales tax would be an inadequate substitute for the loss of corporate income tax revenue and restricted provincial government access to the faster growing personal income tax field.

A Review of Commission Philosophy and Certain Major Recommendations (See Chapter VII)

The Commission by its own admission recommends a taxation system which would redistribute wealth at the risk of sacrificing economic growth. The Commission assigned highest priority to the objective of "equity", a term which is virtually impossible to define. Under its ability-to-pay approach, low income families and individuals "would become net beneficiaries of government", and middle and upper income groups net contributors to government.

We agree with the Commission's suggestion that society is committed to improving the well-being of Canadians having the least economic power. However, we feel that this objective can best be achieved by

attempting to maximize economic growth. Otherwise, it may be extremely difficult for the Canadian labour force to enjoy full employment in the future.

The Commission's approach, which would penalize Canadians for trying to improve their lot, is inconsistent with the education and training policies of various levels of governments. Further, the Commission's comprehensive tax base is a sharp departure from the traditional concept which holds that income, but not capital, should be taxed.

The Government of Alberta is concerned with the Commission's proposal for taxation of capital gains. The Commission admits that existence of such a tax would reduce the attractiveness of petroleum investments. We cannot accept their assumption that the reduced capital in petroleum would be offset by new investment in new businesses. The Commission does not identify these businesses. It is impossible to visualize new businesses locating in Alberta with total annual investments anywhere near $750,000,000, the current level of annual cash expenditures for oil and gas exploration and development.

Taxation of capital gains, as indicated earlier, would also create serious hardships for farmers, ranchers and lower income groups who have attempted to build up estates through home ownership and other forms of savings. The lifetime exemption of $25,000 on realized real property gains on residences and farms is inflexible and unrealistic. The Commission's "offsets" to taxation of capital gains seem inadequate and administratively infeasible.

In countries which have a capital gains tax, revenues from this source make up only a very small portion of total government receipts. Thus it would seem imprudent to introduce such a tax in Canada, a relatively young country which is still in a "period of emergence" and which is short of investment capital. Tax incentives are needed to encourage Canadians to invest risk capital in the development of our resources.

Many of the disadvantages of taxation of capital gains are equally applicable to the proposed taxation of gifts and bequests. The combination of these two taxes could lead to the forced sale of many family-owned

Canadian businesses. The proposal to tax gifts and bequests would nullify the intent of The Alberta Estate Tax Rebate Act. This Act was established as a means to remove barriers and hindrances to the generation of industrial capital in Alberta.

Because of Alberta's heavy reliance on the continual inflow of foreign capital, we oppose the integration proposal which would discriminate against non-resident investment. Integration would also tend to shift investment capital into securities having relatively high current earnings and away from high-growth low-earnings securities. Such a shift could make it very difficult to finance development of Alberta's natural resources.

One of the most serious impacts resulting from implementation of the integration proposal would be losses of some existing tax revenues for an indeterminate period. The Commission did not seem to give adequate consideration to this serious problem.

Other major recommendations of the Commission have inherent weaknesses or disadvantages. For example:

1. the family unit concept would expose members of the unit to double taxation under certain conditions;

2. the limitation of retirement plan programmes to an absolute dollar amount is unrealistic, in view of long range inflationary tendencies, particularly for many young persons entering our labour force;

3. the availability of rapid capital cost allowances to small businesses to offset the impact of a single 50 per cent corporate tax rate would be of no benefit to many service companies presently in the 21 per cent tax bracket. Since many such companies have little investment in fixed assets the rapid capital cost allowance would be of no benefit.

4. proposed taxation of foreign income of Canadian companies seems unrealistic since it would tend to discourage foreign investment by Canadian companies. In the long run such investment should benefit our balance of payments position. Further, such a proposal could force certain companies to relocate their head offices outside Canada.

Many of the Commission recommendations, if implemented, would pose serious administrative, bookkeeping and valuation problems for taxpayers, corporations, and various government departments.

In summary, the Government of Alberta recommends rejection of a number of the major recommendations of the Royal Commission on Taxation. In addition, we have serious reservations about others. Much of the philosophy underlying the Commission's Report is in direct conflict with that of the Government of Alberta, as outlined in our recent White Paper on Human Resources Development.

The present Income Tax Act should be revised as necessary beginning with major matters. Loop-holes and obsolete or unattractive features of the present Act could be corrected without resorting to the proposed system with all its disadvantages and uncertainties.

We would like to make a recommendation concerning procedures for changing our existing Income Tax Act. Changes affect all personal and corporate taxpayers and all levels of government in Canada. Therefore, we feel that before tax proposals are submitted to Parliament they should be reviewed by a truly representative body of experts including recognized Canadian tax authorities from the legal and accounting professions, from industry, commerce, trade unions and all levels of government. We feel such a step would help to avoid the problems which developed as a result of the disproportionate representation of some regions of Canada and some segments of our economy which were evident in the sizeable staff retained by the Commission. Adoption of this recommendation should assure that proposed changes in the Act are appropriate to Canada's national and regional requirements.

Chapter II

THE IMPORTANCE OF NATURAL RESOURCES TO THE ECONOMIC DEVELOPMENT OF ALBERTA

This Chapter briefly describes Alberta's natural resource base and the major role utilization of these various resources has played in the economic development of the Province. An understanding of Alberta's resource base and historical economic development is necessary in order to appreciate the serious impact which implementation of certain recommendations of the Royal Commission on Taxation would have on the Province's future development and upon revenues accruing to the Government of Alberta.

Natural Resources of Alberta

Alberta is blessed with large areas of rich agricultural and forest lands, and relatively large reserves of many important minerals including crude oil, natural gas, coal, gypsum, iron ore, limestone and sulphur.

1. Agricultural Lands

Improved or unimproved farm land makes up 47 million acres or about 30 per cent of Alberta's total land area. This farm land is equivalent to about 27 per cent of Canada's total farm area[1/], or second only to Saskatchewan which accounts for 37 per cent of the Canadian total.

In 1966, commercial farms in Alberta (that is farms of one acre or more with agricultural product sales of $2,500 or more per year) numbered nearly 50,000 and represented over 40,000,000 acres.

1/ "Western Canada" Land of Resources published by the Bureau of Statistics, Department of Industry & Development, Province of Alberta, shows 73,800 square miles of occupied agricultural land, equivalent to 47,232,000 acres. See Appendix Table A.

2. Minerals

Large reserves of a number of important minerals are found within the borders of Alberta. In the case of crude oil, natural gas, sulphur and coal, Alberta's reserves make up a major portion of total current Canadian reserves of these minerals, as indicated by the following tabulation:

Mineral	Alberta's Share of Total Canadian Reserves
Crude Oil - Probable Remaining[2/]	86%
Natural Gas Liquids - Probable Remaining[2/]	93%
Natural Gas[2/]	81%
Sulphur[3/]	97%
Coal[4/]	48%

3. Forest Resources

Productive forest land makes up 117,000 square miles, or just under 50 per cent of total land area in Alberta. Forestry production, however, accounts for less than one per cent of net value of general industry production.[5/] Despite this low forestry production, Alberta has significant reserves of standing timber.

Approximately 13 per cent of Alberta's land area consists of National Parks, Indian Reserves, Provincial Parks and Provincial forest reserves, most of which occupy forest land. Exploitation of mineral and forest reserves found within National Parks is prohibited.

2/ Source: Based on data included in the 1966 Canadian Petroleum Association Yearbook; Probable reserves also include proved reserves. See Appendix Table B.

3/ Source: Based on data included in a speech to the Canadian Institute of Mining & Metallurgy by Mr. H. W. Manley, President, Jefferson Lake Petrochemicals of Canada Ltd., September 27, 1967.

4/ Source: Alberta's Economic Prospects: Government of the Province of Alberta. A submission to the Royal Commission on Canada's Economic Prospects, page 85.

5/ Source: Western Canada Land of Resources, op. cit.

Economic Development of Alberta

Economic growth in Alberta has resulted primarily from development of our natural resources. As expressed by Hanson[6/]:

> "The Province of Alberta . . . is a region with a high ratio of land to people. Consequently, the economic progress of the province hinges upon the degree of utilization of its physical resources."

Initially, economic development of Alberta was related primarily to farming and ranching, which accounted for rapid immigration to and settlement of the Province. Most of the readily accessible homestead land in the Province was settled prior to 1911. By 1911 agriculture employed 70 per cent of the labour force.[7/] The remainder was employed primarily in other occupations serving agriculture. Personal income was subject to wide variations owing to the impact of unfavourable weather, market conditions or pests on farm and ranch production. For all practical purposes, Alberta had a one-industry economy.

Settlement in more remote areas continued until the 1929 Depression which precipitated a significant drop in personal income and personal income per capita. Population growth also slowed. Alberta's growth was minimal until the outbreak of World War II, at which point the population began to rise once again coincidentally with the nation's general economic recovery.

However, a post World War II oil boom, initiated by the 1947 discovery of crude oil at Leduc, gave the major impetus to the Alberta economy from that point to the present.

The majority of our natural resources production is consumed in other parts of Canada or in export markets. In order to compete in these markets, Alberta producers must absorb the effect of high transportation costs on outgoing production owing to the Province's land-locked location. On

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6/ Dynamic Decade by Eric J. Hanson, Professor of Economics, University of Alberta, page 17.

7/ Caves and Holton, "The Canadian Economy", Harvard Economic Series, Harvard University Press, page 199.

in-bound manufactured goods used in processing these resources, this transporation disadvantage must be absorbed by Alberta's consumers or producers. Despite these handicaps, our rate of economic development during the past twenty years has been more rapid than that of Canada, as a whole, largely because of the direct and indirect benefits from natural resources development.

The balance of this Chapter briefly traces this development in terms of growth in population, employment and labour force, personal income, and net value of general industry production. The contribution made to economic development by agriculture, petroleum and natural gas, manufacturing and construction activity in the Province is high-lighted. Reference is made to major sources of Government revenues, which are obviously dependent on maintenance of a healthy and diversified Provincial economy.

1. Population Growth[8/]

Alberta's population grew from 608,000 in 1926 to 803,000 in 1946, equivalent to 1.4 per cent per year, the same average growth rate experienced during this period in the rest of Canada. By 1966, Alberta's population had spurted to 1,463,000, equivalent to an average annual growth rate of 3.0 per cent. By contrast, the annual growth rate to 1966 for the remainder of Canada was only 2.4 per cent.

The rural to urban population shift which was quite pronounced in earlier years has noticeably declined. In 1966, rural population (consisting of farm and non-farm categories) totalled 452,000 or 31 per cent of total Provincial population. Rural population accounted for 52 per cent of total Alberta population in 1946, and 37 per cent in 1961. The 1966 farm population of 278,000 compares with 286,000 in 1961. Rural non-farm population of 174,000 compares with 203,000 in 1961. Part-time or full-time employment opportunities offered by the petroleum industry to rural residents have contributed to stabilization of population size in the rural areas.

8/ Source: Canada Year Book, selected years.

2. Employment and Labour Force[9/]

Since World War II farming and ranching operations in Alberta have become increasingly mechanized. Labour force employed in agriculture, as a consequence, decreased from 121,500 in 1946 to 94,000 in 1966. During this same period, the Province's total labour force increased substantially, from 302,600 to 560,000, reflecting increased employment opportunities mainly resulting from operations of the petroleum industry. Increased employment in services, wholesale trade, retail trade and construction accounted for about 75 per cent of the total increase in employment over this period. During this postwar period, the unemployment rate for the Prairie Provinces has been consistently lower than that experienced for Canada as a whole.

3. Personal Income[10/]

The most significant change in personal income in Alberta over the 1946 to 1966 period was the change in relative importance of wages and salaries, which, (in terms of constant dollars) increased from 53 per cent to 74 per cent of total personal income.

It is certain that personal income in Alberta would not have grown at the same rate as the remainder of Canada nor would it have broadened as much during the postwar period if petroleum industry activities had not offset declining employment in agriculture.

4. Net Value of General Industry Production[11/]

In 1946 agriculture directly accounted for nearly 60 per cent of total Net Value of General Industry Production. By 1966, the net value of agriculture had more than doubled, to $630 million, but its direct contribution was only 23 per cent of total Net Value of General Industry Production. Net value of mining production (primarily oil and gas) increased to $850 million, nearly 18 times greater than 20 years earlier. By 1966, value of mining production accounted for about one-third of the Provincial total.

9/ Source: Province of Alberta.

10/ Source: Based on Dominion Bureau of Statistics data.

11/ Source: Based on Dominion Bureau of Statistics and Alberta Bureau of Statistics data. See Appendix Table C.

Alberta's relatively greater dependence on natural resource industries is evident from the fact that in 1966 agriculture, forestry, fisheries, trapping and mining, together comprised 55 per cent of Alberta's total net value of production compared with less than 20 per cent of total net value of production in the remainder of Canada.

Growth in manufacturing and construction, the other major categories, have been closely tied to natural resources development.

5. Major Industries in Alberta

Agriculture

In 1966, about 17 per cent of Alberta's total work force was directly employed in agriculture. This is double the national average. Alberta commercial farms presently average 840 acres in size, approximately twice the average size of farms in other parts of Canada (which would still be heavily weighed by the large farms of Saskatchewan).

Livestock and field crops are the most important segments of the Province's agricultural economy. For example, Alberta raises approximately 29 per cent, 26 per cent and 32 per cent of Canada's total population of beef cattle, swine and sheep, respectively.

Wheat, oats, barley and tame hay together account for over 80 per cent of gross farm value of field crops. Alberta farms account for a significant portion of total Canadian value of production of these crops, as tabulated below for 1965:

	Alberta's Share of Total Canadian Production
Wheat	23.6%
Oats	25.0%
Barley	53.5%

Agriculture also contributes to growth in certain of our manufacturing industries, particularly foods, beverages, and agricultural implement manufacturing. In 1961, the "food and beverage products" category accounted for $95.2 million or over 27 per cent of Alberta's net value of manufacturing.[12/]

12/ See Appendix Table D.

Approximately $71 million of the food and beverage total was related to the processing of agricultural produce (i.e., meat packing, dairy products, canning, grain mills, etcetera).

Agriculture has benefited from the rapid development of the petroleum industry as a consequence of improved transportation facilities, sizeable contributions to municipal and provincial revenues, payments to farmers for mineral rights, landleasing, etcetera (which have helped farmers finance their operations; including equipment, land, and livestock acquisitions).

Petroleum and Natural Gas

Alberta production of liquid hydrocarbons increased from very modest levels in 1946 to a current level of 250 million barrels per year, which is equivalent to 65 per cent of total refinery runs in Canada. Total deliveries of Alberta natural gas have also increased dramatically, reaching 890 billion cubic feet in 1966. These deliveries, equivalent to 140 per cent of current Canadian consumption, demonstrates the sizeable export market for Alberta natural gas.

In 1966, value of Alberta production of crude oil, natural gas and sulphur was estimated at $721 million. This amount does not include value of natural gas liquids production, which in 1966 amounted to over $90 millions. In recent years, the value of production of these petroleum industry commodities has accounted for as much as 90 per cent of the total value of Alberta's mineral production. In 1947, the value of production of these minerals accounted for only 36 per cent of the Alberta total.[13/]

Mineral production has played an increasing role in the overall Canadian economy and more particularly in the economy of Alberta in recent years. To illustrate, value of mineral production in Canada grew at a compound annual growth rate of 9.3 per cent compared with an average annual increase of 7.3 per cent in Canada's Gross National Product between 1949 and 1964.[14/] The value of Alberta's mineral production

13/ Source: Prepared from data in Canada Year Book and Financial Post Survey of Oils. See Appendix Table E.

increased from 13 per cent to 22 per cent of total Canadian mineral production during this same period.[14/]

Since financing of exploratory activities by exploration and producing companies traditionally depends to a large extent on funds developed from operations, the value of this oil and gas production is of major significance to the industry's continued development. In 1966, total cash expenditures by the exploration and producing phase of the industry in Alberta totalled $743 million[15/], which was allocated as follows:

	(millions of $)
Exploration	$319
Development Drilling	90
Capital Expenditures[16/]	60
Operation of Wells	78
Natural Gas Plants	76
Taxes (excluding income taxes, royalties and other expenses)	120
	$743

The direct petroleum industry investment is important because of its overall stimulation of economic activity in Alberta. It is indirectly responsible for a major portion of the investment in trade, finance and commercial services, housing, etcetera.

Studies prepared by economists clearly indicate the significant multiplier effect or contribution of the petroleum industry to the overall

14/ Source: Prepared from Canada Year Book data. See Appendix Table F.

15/ Canadian Petroleum Association - Statistical Year Book - 1966. It is recognized that all funds generated from production in Alberta are not necessarily re-invested in the Province. Also, funds generated in 1966 are probably re-invested in 1967 and thus the comparison of 1966 expenditures against 1966 income is not strictly realistic.

16/ Includes oil and gas field equipment plus secondary recovery and pressure maintenance installations.

Alberta economy. For example, a study by Dr. Eric J. Hanson of the University of Alberta indicated that the petroleum industry has virtually doubled employment in Alberta between 1946 and 1966.[17/]

Heavy expenditures required by the petroleum industry on goods and services have attracted many new business operations to the Province which have in turn created employment opportunities that would not have been possible otherwise.

Manufacturing businesses which have moved into Alberta to serve the petroleum industry have been many and varied and have included pipe mills, equipment manufacturers and fabricators. Many opportunities in professional, financial and service functions oriented to the needs of the petroleum industry have also developed. Because of the nature of exploration and development activities, the local economies of many small communities have benefited from the petroleum industry. Repair shops, trucking companies, fuel dealers and many retail and wholesale operations in these small communites directly or indirectly owe a large part of their livelihood to petroleum exploration and development.

Construction

The total gross value of construction in Alberta (including new construction and repairs) rose from $556 million in 1953 to $1.21 billion by 1966.[18/] The petroleum industry makes a very significant direct contribution to construction activity in Alberta. In 1966, it accounted for $347 million or 28 per cent of total gross value of construction activity, which compares with only 3 per cent in the remainder of Canada. This does not include the amount contributed to residential, industrial, commercial, road or electric power construction.

17/ Regional Employment and Income Effects of the Petroleum Industry in Alberta, by Dr. E. J. Hanson, presented to the American Institute of Mining, Metallurgy and Petroleum Engineers, March 1966, New York.

18/ Source: Dominion Bureau of Statistics. See Appendix Table G.

Primary industries and construction are much more important (relatively speaking) to total public and private investment in Alberta than in the rest of Canada. In 1966, these investments totalled 38 per cent of total public and private investment in Alberta but only 16 per cent in the rest of Canada.

Manufacturing

Chemical and metal fabricating industries, both of which are allied to or heavily dependent on the petroleum industry, have shown the strongest relative growth in the postwar period. Between 1951 and 1965 chemicals and chemical products increased eightfold, to $50 million and metal fabricating nearly fivefold, to $96 million. Conversely, the food and beverage industry, the most important single category, increased only 2.5 times to about $133 million by 1965.

Alberta is more oriented towards the processing of agricultural and non-metallic mineral produce than Canada generally. In 1964, food and beverage manufacturing industries constituted 28 per cent of Alberta's net value added in manufacturing compared with 15 per cent for Canada as a whole.

Non-metallic mineral products, petroleum and coal products and chemicals and chemical products accounted for 28 per cent of value added in Alberta compared with 13 per cent in the remainder of Canada.

Electric Power Generation

The oil and gas industry has created a rapid growth in the demand for electric energy in Alberta. In part, this demand arises from the exploration for, production and transportation of oil and gas. In addition, refineries and large petrochemical operations have been established. These activities have spawned others: new cement plants, steel fabricating mills, expanded road building programs, and a major boom in commercial and residential construction are only a few among the many.

Over the years the economics of generating and transmitting

electric power have changed greatly. The power demands stimulated by the oil and gas industry have enabled the Province to benefit from these improved techniques resulting in economies to all Alberta power consumers. The extent to which this has occurred can be better appreciated when one realizes that more than 40 per cent of Alberta generating facilities is less than 5 years old and more than 60 per cent is less than 10 years old.

The form in which these economies have occurred in Alberta consist of the following:

(a) Large thermal-electric units using low cost fuels have been installed for operation at high use factor.

(b) Large hydro-electric units are operated over peaks taking advantage of fast start-up, remote control and low incremental cost of added units at pre-existing storage developments.

(c) Development of power facilities in conjunction with storage developments to alleviate pollution on the North Saskatchewan River.

(d) Development of Alberta coal resources for thermal plants, through the use of large scale mine equipment and operating techniques.

(e) Development of extensive networks of high voltage transmission lines linking all major Provincial hydro and thermal power plants, thus making possible the orderly and economic development of Provincial energy resources.

(f) Increased density of service area coupled with extensive transmission and distribution networks has resulted in lower transmission and distribution expenses making it possible to reduce price and supply small towns and rural areas that would not otherwise be economic.

Accordingly, it can be said that the oil and gas industry has materially benefited Alberta through lowering the cost of electric energy to Alberta residents.

6. <u>Government Revenues</u>

Since 1946 the Government of Alberta and various municipal governments have become increasingly dependent on direct and indirect revenues resulting from operation of the petroleum industry. For example, direct petroleum industry contributions in the form of crown reserve

purchases, fees, rentals and royalties have been in the order of 50 per cent of net Provincial Government revenues in recent years.[19/] This percentage excludes Alberta Government revenues from taxation of individuals and corporations directly involved in the petroleum industry as well as those in the secondary and tertiary levels of industry that depend heavily on the petroleum industry.

If Alberta had not had a petroleum industry, the Province would have required Federal Government assistance through equalization payments, grants-in-aid and price support programs. To the extent that this has freed Federal revenues for distribution to other provinces, the other provinces obviously have also benefited from the petroleum industry. Without the oil boom the Prairies could have been a "depressed area", particularly in years when the agriculture sector dropped off for reasons of weather, export markets, etcetera.

At the present time, the Province of Alberta receives no assistance from the Federal Government in the form of tax equalization and stabilization payments. Until very recently, existing sources of Alberta Government revenue have been sufficient to match or exceed expenditure requirements. However, in the fiscal year ending March 31, 1967 revenues fell behind expenditures. For the fiscal year ending March 31, 1968, estimated expenditures are also in excess of estimated revenues.

The prospect of an increasing deficit means that some combination of increased taxation, reduced expenditures and debt financing will likely be necessary to balance future Provincial Government budgets in Alberta. Implementation of certain Royal Commission recommendations can only accelerate and augment the Alberta Government's fiscal problem. Chapter VI contains further elaboration of this point.

19/ See Appendix Table H.

Summary

The growth and diversification of the economy of Alberta during the past 20 years have resulted from the activities of our two major resource industries - agriculture and petroleum. Without the sizeable investment by the petroleum industry in this period, our population growth would almost certainly have been minimal since mechanization and increased productivity of agriculture resulted in reduced labour force requirements. Directly or indirectly these two industries have made major contributions to Provincial and Municipal government revenues.

Any taxation programs or other actions which serve to adversely affect these resource industries or other industries or services which they support in a total or partial way is certainly not in the Provincial or national interest. Creation of a "recessed" area as a result of implementation of such programs could only result in a greater burden on Canadian corporate and individual taxpayers. Such policies are in direct conflict with the terms of reference and objectives of the Economic Council of Canada.

Chapter III

THE IMPORTANCE OF ALBERTA'S ECONOMIC DEVELOPMENT TO CANADA

Three fundamental factors underline the national importance of Alberta's economic development:

1. Alberta's main industries, agriculture and petroleum, are extensively integrated into Canada's pattern of commercial development;

2. Both industries provide a variety of products of strategic importance from the standpoint of national welfare and security; and

3. Sound economic development within Alberta has led to the present position whereby other parts of Canada are not required to support Alberta's economy through government-directed redistribution of wealth. In fact, other provinces have benefited from Alberta's economic development.

The relevance of these three points to the national interest is concisely discussed under separate headings.

1. Commercial Importance of the Agricultural and Petroleum Industries

Agriculture and petroleum are two very important natural resource industries. Both create regional employment and income opportunities in the secondary and tertiary levels of industry. This generative effect also extends to the national level because of the processing, transportation, handling and distribution requirements to convey the products of these industries to domestic markets across Canada and to export markets.

The flow of these commodities to market is extremely important to the stability of economic growth throughout Canada. Regional development in Western Canada has substantially increased the market for Eastern Canadian manufactured goods. An incremental growth factor has been created in this market through accelerated mechanization of Prairie farming and ranching operations and a trend towards increased use of Canadian-manufactured machinery and equipment by the petroleum industry.

A sample analysis of East-to-West rail traffic gives some indication of the increasing importance of the Western Canadian market for certain Eastern Canadian manufactured products during the past five years. For

instance, the rail revenue for transporting selected commodities such as agricultural implements and parts; motor vehicles and parts; iron and steel pipe and fittings; chemicals; building materials; machinery; electrical equipment; appliances; etcetera, was compared for the period 1961 to 1966. Over this period, the East-to-West rail revenue appears to have risen nearly 50 per cent.[1/]

Regarding Western Canadian agricultural and petroleum industry production, the major portion of production from these industries is developed for consumption in Eastern Canadian and export markets. In the crop year 1964 to 1965, 482 million bushels of Canadian grain (all types) were exported and 697 million bushels were consumed domestically. In 1965 to 1966, exports totalled 680 million bushels and domestic consumption 727 million bushels. The following tabulation which summarizes loadings and unloadings of certain grains carried by rail in 1965, gives some indication of the importance of grain movements.

Revenue Freight Carried by Railways - 1965[2/]

(Thousands of Tons)

Location/Commodity	Loaded[3/]	Unloaded[4/]	Deliveries to U.S. Rail Connections
Prairie Provinces			
Wheat	15,149	1,654	-
Oats	1,008	103	-
Barley	1,906	229	1
Wheat Flour	650	77	3
Ontario and Quebec			
Wheat	1,679	9,467	181
Oats	242	961	90
Barley	218	1,421	28
Wheat Flour	548	589	345

1/ Based on data contained in the Board of Transport Commissioners for Canada, Waybill Analysis 1961 and 1966.

2/ Dominion Bureau of Statistics - Railway Freight Traffic. The net unloadings of prairie provinces grain in British Columbia and the Maritimes are not shown in this tabulation.

3/ Includes imports at lake or ocean ports.

4/ Includes exports at lake or ocean ports.

The following tabulation shows the major consumption breakdown for Alberta petroleum industry production during 1966.

Product	Per Cent Consumed by Major Market Area[5]			
	Western Canada	Eastern Canada	Export	Total
Crude oil and equivalent	35.5	22.9	41.6	100.0
Propane and butane	62.9	8.1	29.0	100.0
Natural Gas	34.5	27.1	38.4	100.0
Sulphur	35.3	-	64.7	100.0

These tabulations briefly illustrate the magnitude or relative importance of these commodity flows.

In addition, agricultural and petroleum industry exports make a significant contribution to Canada's international balance-of-payments.

In 1965, Canada's total export trade was valued at $8.5 billion. Of this total, cereal grains and preparations accounted for $1.2 billion and petroleum industry products for $0.4 billion or nearly 19 per cent of total exports.[6]

The following tabulation illustrates Alberta's important role in producing cereal grains and petroleum industry products in 1965.

Alberta's Share of Total Canadian Production[7]

Cereal Grains	Per Cent
Wheat	23.6
Oats	25.0
Barley	53.5
Petroleum Industry Products	
Crude Oil	63.0
Natural Gas	81.7
Natural Gas Liquids	94.0
Sulphur	96.8

5/ Compiled from Alberta Oil & Gas Conservation Board, Statistics Summary, 1966.

6/ Dominion Bureau of Statistics, Canada Year Book, 1967.

7/ Alberta Wheat Pool and Canadian Petroleum Association, Statistical Year Book, 1965.

Over the past 20 years, Canada's net balance of merchandise trade has been somewhat erratic. However, a stabilizing general upward trend has developed from the deficit position in 1956 of $728 million to the 1966 surplus position of $380 million. Underlying this upward trend has been the steady improvement in the net balance of trade on petroleum industry products (including sulphur) from a 1956 deficit of $324 million to a 1966 surplus of $16 million. In addition, wheat exports amounted to $513 million in 1956, $1,024 million in 1964 and $840 million in 1965.

2. Strategic Importance of the Agricultural and Petroleum Industries

In addition to the economic importance of agriculture and petroleum to Canada, there are other aspects of their value that are not definable in economic terms.

For instance, recent food shortages in foreign countries are said to be an indication of more severe and widespread problems of this nature than can be expected in the future resulting from the rapidly expanding world population and limited arable land. At the moment, Canada is self-sufficient in cereal grains and the variety of products derived therefrom. Also, the country maintains an exportable surplus of grain. Canada's vast areas of arable land combined with climatic conditions favourable to grain production are natural assets that will assume increasing value in view of the growing concern over world food supply. This country should at least be in a relatively better position to satisfy its own needs than many other nations and possibly in a position to help alleviate some of the food problems of less fortunate nations.

Regarding petroleum, the evident instability of foreign supplies underscores the advisability of maintaining strong domestic sources of supply. From a national security standpoint, it would indeed be unwise to become too vulnerable to the uncertainties inherent in foreign supply.

International conflicts such as World War II, the Korean War, the 1956 Suez Crisis and, more recently, a second crisis in the Middle East plus an escalation of the war in Vietnam, have occurred with enough frequency to emphasize the need for concern over national security. Each of these conflicts has disrupted or has threatened to disrupt essential energy supplies throughout the Free World for brief-to-prolonged periods of time.

Canada's abundance of hydrocarbon energy supply makes it unnecessary for this country to rely too heavily on foreign sources providing we produce the proper climate to induce the investor to take the risk involved in exploration. In fact, our resource potential is such that the nation could be essentially self-sufficient in energy.

Another important consideration is the close correlation between a country's efficient consumption of energy and its economic growth.[8/]

The relative importance of the petroleum industry in Canada's past, present and future energy supply is shown on the following table:

Canada's Energy Supply Pattern[9/]

Energy Source (as a per cent of total)	1945	1965	1985
Petroleum	21	54	49
Natural Gas	3	18	25
Coal	57	15	12
Wood	12	3	1
Hydro Power	7	10	7
Nuclear Power	-	-	6
Total	100	100	100

8/ Royal Commission on Canada's Economic Prospects - Canadian Energy Prospects by John Davis, March 1957, pages 20 and 21.

9/ Address by J. Davis, Parliamentary Secretary to Minister of Energy, Mines and Resources, to a Canadian Institute of Mineral and Metallurgy meeting on May 26, 1967.

This projection indicates that petroleum and natural gas should continue to supply nearly 75 per cent of the nation's energy needs. Without an indigenous supply of these petroleum industry products, Canada would either have to import a foreign supply or seek alternative domestic sources of energy to the extent feasible.

3. The Relationship of Alberta's Economic Stability and Federal Government Assistance

The Federal Government provides assistance to various areas in Canada lacking the financial, human or natural resources to support necessary regional development. To the extent any area is capable of reducing or eliminating its need for federal assistance, commensurately more funds will be available for distribution to areas with a greater need.

Economic growth not only benefits individuals and corporations but all levels of government as well. As the tax base enlarges, so does the fiscal capacity of government. Chapter II of this submission shows the stimulating effect of agriculture and petroleum on Alberta's economy and the large contribution of the petroleum industry to the Provincial Treasury. In this sense, Alberta's economic growth and development, particularly within the past ten years, has relieved the Federal Government of certain regional responsibilities and reduced the overall burden of the Canadian taxpayer. Despite a rapid increase in population, Alberta's demands on federal funds relative to those of other provinces have been decreasing in recent years. Although this trend may not continue indefinitely, it has freed federal funds for distribution to other provinces or for other federal uses.

Regardless of whether the Government of Alberta is able to maintain such a relatively low level of financial dependence on the federal government in the future, Alberta requirements can be minimized by preserving the economic stability of the Province's key industries - agriculture and petroleum.

Chapter IV

THE IMPACT OF COMMISSION RECOMMENDATIONS ON FARMING AND RANCHING OPERATIONS

Agriculture's important contribution to Alberta's economy in terms of net value of production and employment was highlighted in Chapter II which also focused on the multiplier effect of agriculture on secondary industry. Nearly 30 per cent of the total value of Alberta's manufacturing activity is derived from food and beverage processing. The processing of agricultural produce makes up the bulk of this 30 per cent share. The national importance of the industry was discussed in Chapter III.

The Commission has made some recommendations which refer specifically to agriculture[1/] and others that would have a severe impact even though they are not necessarily directed at the industry. The following recommendations in particular would create serious problems for farmers and ranchers:

1. the proposed conversion from the present "cash" to an "accrual" method of calculating taxable income;

2. the proposed capital gains tax (at full tax rates) that would be imposed on gains realized from the disposition of farm property; and

3. the proposed inclusion of gifts and bequests in taxable income.

Conversion to an accrual system would seriously complicate accounting procedures and increase immediate tax exposure. Further, the capital gains tax and inclusion of gifts and bequests in taxable income would increase the tax exposure resulting from any transfer of assets in the farming or ranching operations to a point where an eventual disintegration of existing units-of-operation would become inevitable.

1/ Report of the Royal Commission on Taxation, Volume 4, Chapter 25, page 439.

The purpose of this Chapter is to describe the effect these recommendations would have on Alberta's farming and ranching operations. General background information on the nature of agriculture in Alberta and the apparent basis for these commission recommendations are provided in this Chapter.

Farming and ranching are relatively high risk operations. They are vulnerable to numerous uncertainties of nature including such uncontrollable factors as hail, frost, drought, lack of sufficient hours of sunshine to ripen crops, soil deficiencies, etcetera. The effects of these factors, individually or in combination can wipe out a crop in a given year. Extreme cold and snowfall can cause the death of livestock.

Also, markets for farm produce are highly variable. International wheat sales to Communist countries have greatly expanded in recent years. However, export sales must be considered vulnerable over the long-term. Prior to development of these incremental export markets, excessive inventories were building up. Inventories are still substantial (i.e., currently standing at about twice the level of annual sales).

Individual enterprise still predominates in agriculture in contrast with the current trend towards large consolidated operations in many other industries. This small base of operation provides an additional element of economic risk.

The Commission did observe that the combined effect of the small base of operation and the uncertainties of nature and markets should be given consideration in the taxing of farming income.

However, the Commission expressed concern that the special tax treatment accorded farming operations has led to "significant inequities, anomalies and loopholes, and to administrative problems".[2/] The Commission pointed to a number of factors, including the following, which it implied now reduce the uncertainties of nature and markets:

1. the increasing size of the farm unit;
2. the increased technical assistance from Government authorities;
3. improved marketing arrangements; and
4. the increased use of scientific knowledge and business methods.

2/ Volume 4, Chapter 25, page 440.

Despite recent improvements in farming techniques, scientific technology has not removed, or even reduced, the unpredictable effect of weather on crops and livestock. Also, soil productivity, for instance, can only be improved within certain limits. Consequently the Government of Alberta concludes that the relative degree of risk between farming and other types of business remains essentially unchanged.

A number of the Commission's recommendations, if implemented, could have a pronounced effect on farming operations. In some cases, the Commission recognizes that certain hardships may be created for the farmer.[3/] However, it contends that other provisions under the proposed tax system would mitigate, to some extent, the impact of the recommendations.[4/] Any hardships still incurred beyond the mitigating effect are presumably justified in the interest of achieving the Commission's interpretation of equity. There are other cases where there has been little or no recognition given to the impact of specific recommendations on the agricultural industry.[5/] The general impression created by the Commission is that the overall impact of its recommendations affecting farming operations will not be great.

3/ Conversion from the "cash" to "accrual" basis of calculating income would mean the immediate imposition of taxes on inventories and accounts receivable less accounts payable.
Farm property transferred between related persons should be deemed to have been sold at fair market value (i.e., requiring the present owner to recapture depreciation). If the sale price is less than fair market value the difference should be treated as a gift.

4/ The fair market value of land as at the transition date could be reduced by the amount required to put a farming operation on the accrual basis. This would defer tax payment on the amount of the accrual adjustment until the farm is sold. The averaging of income over five years would be permitted on the same basis to be allowed all taxpayers. (The present limited provisions applicable to farmers would be repealed).
The lifetime exemption of $25,000 on gains realized from the sale of residential property would also be extended to farm property.

5/ The proposed inclusion of all capital gains, gifts and bequests in a comprehensive tax base taxed at progressive rates.

Regarding tax revenues from the agricultural industry under the proposed tax system, the Commission concluded that the overall amount received should not change appreciably and that "on balance, there should be some increase".[6/]

We believe that reliance on national averages combined with an insufficient recognition of many practical problems relating to the agricultural industry led the Commission to a number of invalid conclusions and recommendations in this area. It would appear that farmers who barely make a living from their operations will be relatively unaffected by many of the recommendations. Since they are low income earners, tax changes will have little effect on them. However, we do not believe the Commission has adequately anticipated the general result of its recommendations on those farmers and ranchers who pay a reasonable tax on their earnings.

In brief, the proposed changes in tax legislation would increase the tax exposure on any transfer of assets in the farming operation between related persons. The increase would be sufficient to require the person receiving the transferred assets to dispose of part or all of them in order to pay the taxes on such assets received. With respect to taxation of capital gains and inclusion of bequests and gifts in taxable income, the proposed lifetime exemptions of $25,000 and $5,000 respectively would inadequately cushion the impact for many farmers and ranchers.

The result would be to fragment existing economic farming units and severely impair individual initiative. The eventual outcome could be for the ownership of farming operations to be transferred to large and probably non-resident investors.

6/ Volume 4, Chapter 25, page 451.

1. "Cash" Vs. "Accrual" Method of Calculating Taxable Income[7/]

A number of problems would result from enforced conversion to an accrual system of calculating taxable income. The accounting requirements that would be imposed on farm or ranch operators under an accrual method would be much more complex and onerous than those of the present cash system. The need to value inventories (not required under the cash system) would create significant problems since inventory valuation can be extremely complicated for both grain and livestock. The need to include accounts receivable in taxable income would impose an unfair additional tax burden on farmers because of the unusual method of grain payments.

The Commission's concern that the exclusion of inventory results in a serious understatement of farm income under the cash system leads to the recommended change from cash to accrual accounting for any farming operation generating over $10,000 gross revenue annually. Once the accrual method has been implemented there would be no opportunity to revert to the cash method. To cushion the hardship created by this unexpected change in proposed legislation, the Commission further recommends that farmers be permitted to reduce the market value of assets at the transition date by the excess of assets less liabilities on a cash basis. This proposed tax deferral would remain in effect until disposal of the assets.

Market gardening, fruit farming and related types of farming operation would be relatively unaffected by the recommended conversion from cash to accrual accounting. Little or no inventories are involved in these types of farming operations. Disposal of inventory and payment therefor is essentially immediate. However, the effect on cereal crops and ranching operations would be substantial.

Although cereal crops are grown and cattle raised throughout Canada, the major portion of these farming operations are concentrated in Western Canada. Another significant factor in analyzing the impact of the

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7/ Net cash income is basically defined as cash receipts less cash disbursements. In this method of computing taxable income, sales are not recorded until payment is rendered.
The accrual method requires that accounts receivable, inventory, and accounts payable be taken into account as taxable income.

Commission's recommendations is the size of farms in Western Canada. The national average size for commercial farms[8/] is about 510 acres as compared to 840 acres in Alberta. The nature of farming operations on the Prairies requires the larger-sized unit in order to be economically viable. However, the inventory generated by these farms will increase the incremental tax burden brought about by inclusion of accounts receivable in taxable income.

Table 25-1[9/] of the Commission's Report reveals some important statistics which place in perspective the relative efficiency, from a tax revenue standpoint, of Western Canada's farming operations. About 53 per cent of Canada's total commercial farms are located in the four Western Provinces. However, 71 per cent of the taxpaying farmers are located in the West and they contribute 67 per cent of the national tax revenue from agriculture.

The farm size and tax figures just presented show that changes in tax legislation, which would adversely affect farming operations, would bear more heavily on the residents of Western Canada.

(a) Onerous Accounting Requirements

The Commission apparently holds the view that modern farming is now more comparable to a normal business operation and that farmers are "probably already maintaining sufficient information to adjust cash records to an accrual basis".[10/] These generalized assumptions by the Commission are unsupported by the facts. The Farm Management Branch, Alberta Department of Agriculture, confirms that a high percentage of farm records are inadequate even on a "cash" accounting basis.

Requiring farmers to maintain records on an accrual basis would be tantamount to asking them to hire professional accountants. A balance sheet would have to be prepared each year to tie in with the profit and loss account.

8/ Farms of greater than one acre which yield sales of more than $2,500 annually.

9/ Volume 4, Chapter 25, page 439.

10/ Volume 4, Chapter 25, page 442.

There is generally a dearth of bookkeepers let alone qualified accountants in most rural communities. Thus, an extensive educational program would be necessary to familiarize farmers with the accounting techniques used in preparing financial statements. The education program would be required to prevent chaos and even then the results are likely to be uncertain.

(b) <u>Inventory Valuations</u>

Inventory valuation of livestock or grain can be extremely complicated. There is, of course, no problem in costing purchased livestock. However, many ranchers raise their own herds. Any cost assigned to a new calf must, of necessity, be arbitrary. As the animal matures, the incremental cost of raising it is also arbitrary.

Evaluating the cost of grain in inventory is even more complex. As the Commission recognized, market price and cost are two entirely different things. In the case of cereal grains, particularly wheat, international agreements determine prices rather than the normal laws of supply and demand and the cost of production.

The Commission states that the market value of farm inventories was $3 billion at the end of 1963 with livestock accounting for $2 billion of the total and grain, $1 billion. The Commission estimates the <u>cost</u> of this inventory at between $1 and $2 billion with the major portion of the cost being in livestock.

The fact that the cash method of accounting does not require inclusion of these substantial inventories in income is considered a serious void in the present tax system by the Commission. The cost of inventory build up can be deducted immediately under the present system. Under the accrual system, the cost of inventory would eventually be allowed as a deduction at the time of sale. However, the Commission contends that the cash system permits tax deferral which amounts to an "interest free, unsecured loan"[11/] not available to business generally.

It should not be overlooked that farming and ranching are high risk business operations. We believe people engaged in these operations

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11/ Volume 4, Chapter 25, page 441.

should have the opportunity to recover their investment in inventory before being exposed to taxation. In defence of the present system, it can be stated that the immediate write-off provision of the cash system is a major factor in assisting farmers to improve their operation. The deferred tax exposure provides necessary capital and thereby stimulates individual enterprise.

If the Commission envisages costing grain on a basis similar to manufactured products, many real problems could arise. Costs of grain production, such as labour, taxes, interest, rent, gasoline, repairs and depreciation are incurred regardless of crop yield. However, the vagaries of nature cause an extremely wide variation in crop yield. The following tabulation shows that the variation can be very substantial.

COMPARISON OF CROP YIELD VARIATIONS[12/]

	Minimum Yield		Maximum Yield		
Cereal Crop	Year	(Bushels per acre)	Year	(Bushels per acre)	Per Cent Variation
Wheat	1961	10.6	1966	27.7	161
Oats	1961	25.2	1942	51.7	105
Barley	1947	18.6	1966	40.6	118
Rye	1949	7.2	1966	23.6	228
Flax seed	1957	5.5	1965	12.5	127
Rape seed	1950	6.0	1951	18.5	208

In addition to the general year-to-year variations, differences in soil and weather conditions can create variations in yield in the same year even for neighbouring farmers.

Under the normal rules of inventory valuation for the manufacturing industry, inventory is pegged at the lower of cost or market. In years of poor crop yield, a farmer's cost could exceed his selling price. If the manufacturing rules for inventory valuation were applied in these years, farmers wou not even be able to deduct full costs in calculating taxable income.

12/ Compiled from Canadian Wheat Board Annual Report, 1965-66, Table II covering the years 1942 to 1966 inclusive.

are made in the January after at least one full calendar year has elapsed since the date of delivery.

For example, to the extent a farmer delivers his 1965 crop before December 31, 1965, he will not receive his final payment until January, 1967. Deliveries made after December 31, 1965 of any remaining portion of the 1965 crop and any delivered portion of the 1966 crop would create further accounts receivable on hand at December 31, 1966. When a farmer makes delivery before year-end but does not receive initial payment until the next year, his accounts receivable would be based on the full price of the grain and not merely on the final payment.

The following tabulation shows the price variation amongst different types and quality of grain.

Recent General Grain Price Ranges

Wheat	-	$1.65 to $2.00 per bushel
Oats	-	0.70 to 0.90 per bushel
Barley	-	1.15 to 1.25 per bushel

The net receipts to the farmer are 15¢ to 20¢ below these prices as a result of freight and elevator charges. Price variations reflect differences in quality resulting from such uncontrollable factors as weather and soil conditions, etcetera.

Table IV-1 was developed to provide an approximate idea of the amount Canadian grain farmers would have to record in accounts receivable each year under the accrual system. The five-year average shown on the table indicates this amount would be in the order of $300 million. Requiring farmers to bring accounts receivable into taxable income is the equivalent of burdening them with annual interest payments since they would, in effect, be prepaying taxes on monies not yet received. Assuming an average effective tax rate of 19 per cent[15/] and a current interest rate of 7 per cent, farmers would be burdened with annual average interest

15/ Department of National Revenue - Taxation Statistics, 1966 Edition, Part 1, Table 3, page 25. (1964 Taxation Year - Total Tax Payable vs. Taxable Income Assessed).

payments, not now experienced, amounting to $4.0 million.

(d) Accounts Payable

The corollary to accounts receivable is, of course, accounts payable. In most manufacturing or industrial businesses one offsets the other to some extent, though rarely entirely.

The grain farmer's raw materials are really seed and land. Most farmers raise their own seed or buy it in the late winter and it is paid for before the end of the year. There may be a month or two of gasoline or repair bills outstanding. However, the bulk of their payables represent non-expense items such as machinery and bank or mortgage loans.

Hence, there would be very little relief in being allowed to offset payables against receivables.

(e) Unexpected Need for Conversion

The Commission recommends that farmers with gross revenue of less than $10,000 per year could continue to operate on a cash basis. However, once a farmer has converted to the accrual system he must remain on that basis thereafter.

Periodically, a farmer may receive an unexpected, "one-shot" revenue opportunity that would inflate his year's earning over the $10,000 level. For example, a construction company building roads in the area might wish to contract for sand or gravel from the farmer's land. This could place the farmer in an awkward position. If he accepts the construction company's offer, he would not only have to bring any accounts receivable into income, he would also have to evaluate his inventories. The inventories would either have to be brought into income or the value of his land reduced.

2. Capital Gains Tax[16/]

The Commission's proposal to treat farm land as ordinary real estate can only lead to gradual disintegration of these economic units. As a result, it should bear critical examination.

The Commission suggests that its provisions for:

(a) farmers to claim the lifetime $25,000 tax exemption accorded all taxpayers for gains on land disposition, or

(b) claim a deduction for any losses incurred on the sale of farm property,

will, essentially, remove any possible hardship effect on farmers.

At the outset, an important distinction must be made. There is a very real difference between the real estate value of land generally and the productive value of farm acreage.

The normal farm operator acquires land for the purpose of making a livelihood and of enhancing the land's value through a life-long process of capital investment and the efforts of his labour. He is not a land speculator investing solely for the purpose of realizing a capital gain on the appreciation of land value. The normal farm operator hopes to develop a valuable capital asset that can be transferred from one generation to another as an economic unit. The productive value can be maintained only so long as there is incentive to work the land and the economic unit remains intact.

In order for a farming operation to be economic, a certain sized unit-of-operation must be maintained. Although mechanization may be helping more farms to become economic, the cost of mechanizing them requires a larger-sized farm unit to support the increased cost of operation. As mentioned earlier, the average farm size in Western Canada is greater than for the nation generally and a higher percentage of Western Canada farming operations are taxable.

16/ Discussion of the Commission's proposed capital gains tax will be confined, at this point, to considering the effect of including property gains realized from the disposition of farm property.

The Commission fails to acknowledge the role played by inflation in increasing values of land or commodities. Historically, this factor alone has increased values at an average rate of 3 per cent per year. On this basis, land values double every 25 years. To tax gains attributable to inflation is to take away part of the original value. Such a move would contradict the Commission's stated intention that taxes should be allocated according to the changes in the economic power of individuals and families.[17/] The Commission attempts to rationalize this inequity on the basis that there are many with fixed incomes who experience losses who are "unable to protect themselves against it".[18/] We find this line of reasoning hard to justify in cases where the adverse effects can be proven to be substantial.

The farmer is in a rather unique position in that, relatively speaking, he has a greater part of his assets tied up in land than does a manufacturer. For this reason, the impact of inflation is of much greater significance to the farmer.

An indication of the effect on Prairie farmers can be measured in quantitative terms. Reasonably good farm acreage in Alberta is currently valued in the order of $100 to $150 per acre. These values are considered realistic and not excessive. Applying these values to the average Alberta farm size of 840 acres, a current total dollar value of $84,000 to $126,000 per farm is derived. If we assume such farms are worked for about 25 years and are then sold or passed on to relatives, and that a farmer is able to apply a full $25,000 deduction to the gain in value, the remaining taxable gain would be $59,000 to $101,000. These amounts of taxable gain are considered conservative because they do not take into account real increases in value and they have been calculated for a 25 year period which is a relatively short period of time.

In 1966, nearly 16,000 Alberta farms were larger than the 840 acre average and, in many instances, the land values would be higher than the $100 to $150 price per acre. For a 1,600 acre farm valued at $150 per acre, the taxable gain would be $215,000 under the method of calculation discussed previously.

17/ Volume 3, Chapter 7.

18/ Volume 3, Chapter 15, page 349.

Another equally important factor is the effect on farm improvement incentives. Farmers will be reluctant to modernize their operation to improve efficiency if they know it will greatly increase their future tax burden. Improving efficiency and productivity is essential in all industrial development if we are to continue to improve the nation's standard of living. This need is recognized by the Economic Council of Canada. As part of its policy guidelines for economic growth, the Council once again stressed the need "to improve efficiency in the development and utilization of natural resources".[19/]

The income averaging provisions recommended by the Commission will not be adequate to offset the combined effect of taxing inventory, receivables, and capital gains. The impact that will lead to disintegration of present farm units will be twofold:

(a) the sale of assets simply to pay the extra tax burden will become necessary; and

(b) the psychological impact on individual initiative will be most damaging. The incentive to create a valuable asset through individual enterprise will be virtually removed.

3. Gifts and Bequests

One of the most serious effects on farming operations will result from the Commission's proposal to include gifts and bequests in taxable income.

The beneficiary of an estate will be taxed in two ways under the proposed system:

(a) a tax will be imposed on capital gains unrealized by the estate; and

(b) the full value of the estate (less taxes paid by the deceased) must be brought into income by the beneficiary. This amount will also be subject to normal tax rates.

The Commission recommends a five-year income averaging provision to help counterbalance this effect of increased tax exposure under the proposed new system. The Commission appears to conclude that the averaging

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19/ Economic Council of Canada, Fourth Annual Review, September, 1967, page 259.

provision combined with lifetime exemptions of $25,000 on property gains and $5,000 on gifts will cushion any potential hardships created by the new system.

The impact of the proposed recommendations will, in many instances, be severe enough to cause the most economic farm units to break up in order to handle the incremental tax burden. Obviously, the larger a farming operation the more severe will be the effect. The Commission acknowledges that "an evolution has been taking place in farming in recent years, with an increase in the size of an economic farm".[20/] With this increase in size of operation has come a trend to more economic operation. Comparing 1960 and 1964 tax statistics,[21/] it is evident that, despite the downward trend in the total number of farm operators during recent years, the number of taxpaying farmers in Canada has increased (i.e., from 66,916 to 106,614). Over the same interval, average individual tax payments by taxable farmers increased from $326 per capita to $491. These figures suggest farms generally have been improving their efficiency of operation, an objective considered desirable by the Economic Council of Canada. Farm units must be of a certain minimum size in order to operate on an economic basis. We believe this is a prime example where the Commission's concept of equity and the priority assigned to achieving it works directly against the goal of attempting to maximize economic growth. Larger economic units are desirable. The taxation system should not mitigate against formation of such units.

Quite apart from the very damaging effect this will have on individual incentive is the fact that it completely contradicts sound economic principle.

Even under the present tax system, there are cases where farm estates have been split up in order to acquire cash to pay income and estate taxes. Recommendations by the Commission can only aggravate a situation that already creates unnecessary hardship.

At present, a beneficiary receives his bequest with no further payment of tax over and above the estate tax. If cash is not available to pay the estate tax and the estate is composed largely of land and other

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20/ Volume 4, Chapter 25, page 442.

21/ Department of National Revenue, Taxation Statistics 1962 and 1966, Table 3.

assets which are not immediately saleable, the beneficiary may have to borrow from the bank or other sources. The need for this borrowing will be greatly alleviated by the Government of Alberta's estate tax rebate legislation which is discussed in Chapter VII. Revenue received from the sale of inventory by a beneficiary is not taxable under the present system if income tax has been paid by the estate.

The intent of this legislation runs counter to that of the Commission. Although the Commission proposes to eliminate estate taxes as such, the combined effect of the recommended capital gains tax, gift tax and shift to an accrual system of accounting would effectively increase rather than decrease the overall tax burden.

For example, gift provisions under the present tax system enable a farmer to transfer $90,000 in property to a family member over a 20-year period (i.e., $4,000 per year plus a $10,000 lifetime exemption). Under the proposed system, an individual may only receive a lifetime gift of $5,000 and $250 annually.

Another example is the family unit concept envisaged by the Commission which requires a child to be declared independent of the unit at age 21. Regardless of whether property transfer to the child occurs before or after 21, it will be taxable at fair market value (less purchase price paid by the independent). The tax would be imposed at the time of transfer or at age 21 if the transfer took place beforehand. No provision is made to recognize the contribution made by a child to the economic development of the farming operation before reaching 21. If a member leaving the family unit does not reimburse the unit at fair market value for land or other assets acquired from the unit, the differential will be treated as a gift in the hands of the recipient.

Our concern over the compounding effect of these proposed changes in tax regulation can be best illustrated by some simplified examples. Table IV-2 shows the impact of the Commission's recommendations on $50,000, $100,000, $200,000 and $400,000 farm estates. Briefly, the assumptions are that:

(a) the death of husband and wife occurs at approximately the same time causing the estate to pass on to another beneficiary now outside the family unit;

(b) the estate was acquired by the deceased 25 years prior to his or her death;

(c) inflation at the annual rate of 3 per cent doubled the value over the 25-year period;

(d) no capital gains tax was paid by the deceased on this increase in value;

(e) no portion of the lifetime tax exemptions on property gains (i.e., $25,000) and gifts (i.e., $5,000) have been claimed previously; and

(f) the beneficiary takes full advantage of the five-year averaging provisions.

In the composite, these assumptions are considered conservative because:

(a) no portion of the lifetime exemptions were assumed to have been claimed previously;

(b) real estate values have probably inflated the market value of the land higher than the 3 per cent inflation rate; and

(c) the farm estate would, in many instances, have been acquired more than 25 years prior to death.

Despite the conservative bias the annual taxable income of the beneficiary would be increased by substantial to overwhelming amounts.

As stated earlier, the average farm size in Alberta is currently 840 acres. At a moderate land price of $100 per acre, the farm immediately assumes a land value of $84,000. Twenty-five years from now this figure would be $168,000. These figures exclude the value of buildings, livestock, machinery and equipment which for all Alberta farms currently approximate 90 per cent of capital investment in land. This could be considered the overall value of an average economic farm operation in Alberta. However, it should be pointed out that the land only has productive value if the tax system preserves economic incentive.

4. <u>Summary</u>

Recommendations of the Commission cited in this Chapter will severely impair the financial capability and individual incentive of succeeding generations of farmers to expand and improve the economic efficiency of their operations. Existing economic farm units will have to be broken up to pay additional taxes.

The following effects of the Commission's recommendations relating to farming and ranching should be examined.

1. a capital gains tax on gains in market value of farm property from the time of acquisition to the time of disposition;

2. the requirement for a beneficiary to bring gifts and bequests into fully taxable income without sufficient "exemption" relief; and

3. the recommendation to have farmers earning over $10,000 per year convert from a cash to an accrual system of calculating taxable income.

The proposed treatment of property gains, gifts and bequests will severely impair the ability to transfer the assets of farming and ranching operations from one generation to another. The incremental tax burden imposed by the proposed system will, in many instances, be sufficient to cause existing economic units-of-operation to break up.

The proposed conversion from a cash to an accrual basis of determining taxable income will substantially complicate accounting procedures and will also add to the effective tax burden of farming and ranching operations. The cumulative effect of these recommendations will be to:

(a) seriously damage individual incentive and enterprise;

(b) accelerate the trend to urbanization;

(c) create smaller, less efficient units of farming and ranching operation; or

(d) cause ownership of these operations to pass into the hands of large investors.

The Government of Alberta is greatly concerned over the prospective impact of the main Commission recommendations discussed in this Chapter. The averaging provisions and exemptions proposed by the Commission will be inadequate to offset the adverse effect of its recommendations. We would, therefore, strongly emphasize that any revision of the existing tax system must consider the contribution of farming and ranching operations to the national economy, their uniquely hazardous nature and the need to preserve individual incentive and initiative in this area.

Table IV-1

ESTIMATED ACCOUNTS RECEIVABLE

for

MAIN CEREAL GRAINS IN CANADA

Accounts Receivable as at December 31	Cereal Crop	Harvest Year	Delivery Period (Aug. - July)	Volume Delivered (MM Bushels)	Average Final Payment (¢ Per Bushel)	Accounts Receivable (MM $)	Harvest Year	Delivery Period (Aug.- Dec.)	Volume Delivered (MM Bushels)	Average Final Payment (¢ Per Bushel)	Accounts Receivable (MM $)	Total Accounts Receivable (MM $)
1965	Wheat	1964	64-65	523.7	38.2	200.1	1965	1965	173.2	48.2	83.5	283.6
	Oats			38.8	17.7	6.9			20.8	24.8	5.2	12.1
	Barley			71.4	31.1	22.2			43.4	32.9	14.3	36.5
	Total					229.2					103.0	332.2
1964	Wheat	1963	63-64	563.9	48.3	272.0	1964	1964	179.2	38.2	68.5	340.5
	Oats			48.3	9.8	4.7			17.6	17.7	3.1	7.8
	Barley			88.8	22.6	20.1			28.5	31.1	8.9	29.0
	Total					296.8					80.5	377.3
1963	Wheat	1962	62-63	474.3	42.1	199.7	1963	1963	179.4	48.3	86.5	286.2
	Oats			86.2	12.4	10.7			19.3	9.8	1.9	12.6
	Barley			77.6	18.2	14.1			31.2	22.6	7.1	21.2
	Total					224.5					95.5	320.0
1962	Wheat	1961	61-62	298.9	43.7	130.9 1/	1962	1962	181.9	42.1	76.6	207.5
	Oats			24.9	17.3	4.3			32.0	12.4	4.0	8.3
	Barley			56.4	30.2	17.0			26.4	18.2	4.8	21.8
	Total					152.2					85.4	237.6
1961	Wheat	1960	60-61	396.2	41.5	164.4 2/	1961	1961	109.5	43.7	47.9	212.3
	Oats			36.0	14.1	5.1			15.2	17.3	2.6	7.7
	Barley			86.1	8.4	7.2			40.7	30.2	12.3	19.5
	Total					176.7					62.8	239.5

1/ Includes an interim payment of $6.9 million.

2/ Includes an interim payment of $39.3 million.

Source: Prepared from data supplied by The Alberta Wheat Pool.

Table IV-2

TAX PAYMENTS ON FARM ESTATES
UNDER CURRENT AND PROPOSED REGULATIONS*

Components of Taxable Amount	Estate Value ($)							
	$50,000		$100,000		$200,000		$400,000	
	Current	Proposed	Current	Proposed	Current	Proposed	Current	Proposed
Capital Gains	25,000	25,000	50,000	50,000	100,000	100,000	200,000	200,000
Total Taxable Amount	n.a.	25,000	n.a.	50,000	n.a.	100,000	n.a.	200,000
Bequests								
Less: Exemptions								
Gift 1/	80,000	11,250	80,000	11,250	80,000	11,250	80,000	11,250
Property	10,000	25,000	10,000	25,000	10,000	25,000	10,000	25,000
Total Taxable Amount	-	13,750	10,000	63,750	110,000	163,750	310,000	363,750
Total Taxable Amount	-	38,750	10,000	113,750	110,000	263,750	310,000	563,750

* Assuming the deceased acquired the farming operation 25 years prior to death and inflation has caused the initial value to double. Does not include the Province of Alberta's proposed 75 per cent rebate on succession duties. Assumes beneficiary is outside the Commission's concept of the family unit.

n.a. - not applicable.

1/ Current System - Annual gift exemptions of $4,000 over 20 years.
Proposed System - Lifetime gift of $5,000 plus annual gifts of $250 over 25 years.

Annual Taxable Amount 2/								
Capital Gains	n.a.	5,000	n.a.	10,000	n.a.	20,000	n.a.	40,000
Bequests	n.a.	2,750	n.a.	12,750	n.a.	32,750	n.a.	72,750
Total annual five-year average	n.a.	7,750	n.a.	22,750	n.a.	52,750	n.a.	112,750

2/ The Commission recommends a five-year averaging provision not available under the current system. Therefore, payments could be spread over five years as compared to the lump sum payment required now.

Source: Prepared by The Government of Alberta.

Chapter V

THE IMPACT OF COMMISSION RECOMMENDATIONS ON THE PETROLEUM INDUSTRY

The very sizeable direct and indirect contribution of the petroleum industry to the economy of Alberta in terms of employment, value of production, investment and government revenues was discussed in Chapter II. The national importance of the industry was described in Chapter III. The Commission miscalculated the impact of its recommended changes on the petroleum industry and gave insufficient consideration to the effect on the industry itself, on the economic development and welfare of the Province of Alberta and on the nation generally.

In the section of its Report referring to "mining and petroleum" industries,[1/] the Commission stated that most of the arguments advanced (in published materials, in briefs submitted to the Commission, in views expressed at public hearings, or at interviews conducted by members of its staff) in support of special tax provisions, fell into five categories, one of which was the "social and economic benefits" argument.

The Commission discussed "these alleged benefits from tax concessions to the extractive industries"[2/] by observing that the benefits had been dealt with extensively in studies presented to and prepared for the Commission; therefore, it would deal with them only briefly. As a result, the Commission either completely overlooked or gave inadequate consideration to the overall ramifications of these benefits, particularly as they affect the Province of Alberta.

1/ Report of the Royal Commission on Taxation, Volume 4, Chapter 23.

2/ Volume 4, Chapter 23, page 312.

The Commission concluded that:

> ". . . It is by no means obvious that some of the alleged benefits are, in fact, net benefits. Frequently it is assumed that the additional employment, investment and output of the mining and petroleum industries are achieved without cost in the form of reduced employment, investment and output elsewhere in the economy.
>
> A careful review of the many arguments advanced in support of the present concessions to the mining and petroleum industries does not suggest that the economy would be adversely affected by their removal".3/

The Commission further stated,4/ that many of the arguments relating to the social and economic benefits of such "concessions" involve issues that are outside the subject matter of the Report of the Royal Commission. We are unable to accept this suggestion that all issues regarding impact of taxation policy cannot be properly examined. Taxation is a cost to the corporate taxpayer and any significant increase in taxation of the petroleum industry will have a serious impact on economic activity in Alberta.

The Report made virtually no reference to the impact of its recommendations on regional development. Its treatment of regional development was in the narrow context of settlement of the North and subsidization of depressed areas. While the social and economic benefits relating from settlement of the North is an important subject, it is inconceivable that proper treatment of regional development would concentrate on this subject to the exclusion of overall impact on the economy and development of Alberta.

Our analysis of the section of the Report dealing directly with the extractive industries (mining and petroleum),5/ leads us to conclude that implementation of these Commission recommendations could result in a serious reduction in activity by the petroleum industry in Alberta. The impact of reduced activity would indeed be serious for both the residents of the Province and the Government of Alberta.

3/ Volume 4, Chapter 23, page 371.

4/ Volume 4, Chapter 23, page 307.

5/ Volume 4, Chapter 23, pages 265 to 378.

Immediately following is a listing of the major Commission recommendations for future taxation of the petroleum industry. The balance of this Chapter is devoted to a rebuttal of the bases for such recommendations. Chapter VI contains our estimate of the degree to which revenues, currently available to the Government of Alberta from the petroleum industry, would be reduced by implementation of these particular Commission recommendations.

1. Major Commission Recommendations for Taxation of the Petroleum Industry

The major Commission recommendations for taxation of the petroleum industry are:

(a) Immediate withdrawal of the present depletion allowance;

(b) Development costs should enjoy a rate of write-off of 100 per cent during a transitional period of five to ten years, thereafter they should only be eligible for a write-off at the rate of 20 per cent to 30 per cent on a diminishing balance basis;

(c) The three-year tax exemption period for new mines should be withdrawn after a transitional period of five years (this recommendation is of significance to Tar Sands development);

(d) The cost of each petroleum property should be capitalized and written off by amounts relating to the operating revenue derived from the same property, the rate should be up to 50 per cent in the transitional period and 10 per cent to 20 per cent of the operating revenues from the property thereafter; and

(e) All profits made on the disposition of petroleum properties should be included in income in accordance with the Comprehensive Tax Base.

2. Bases for Commission Recommendations for Taxation of the Petroleum Industry

Three broad reasons can be advanced as having contributed to the Commission's recommendations in this area:

(a) a resolute, conceptual bias against tax incentives in any form (since they appear to conflict with the Commission's interpretation of "equity" in a tax system);

(b) an apparent lack of technical knowledge relating to the petroleum industry; and

(c) an insufficient practical understanding of how the industry functions in the economy.

The Government of Alberta has maintained close liaison with the petroleum industry directly and through various Government agencies, such as the Oil and Gas Conservation Board, the Public Utilities Board and the Research Council of Alberta. Through our familiarity with the economics of the industry, we find a number of the opinions and assumptions of the Commission to be unacceptable. Specifically, we feel that Chapter 23 of Volume 4 of the Report and the supporting study "Taxation of Mineral Industries"[6/] attempted to establish recommendations based on application of certain economic theories which have little, if any, practical application to actual economic conditions.

These theories do not recognize external forces which influence the petroleum industry. It is regrettable that there was insufficient qualified representation from Alberta on the staff of the Royal Commission. Much of the analysis reflected in the Report was based on erroneous assumptions which reflect an inadequate understanding of the petroleum industry. Tax incentives are granted to the U.S. domestic and foreign oil producers. As a result Canadian tax policies must give appropriate consideration to such external forces, since a large portion of Canadian crude oil and natural gas production is sold in U.S. markets where the establishment of price is outside our control.

At various points throughout its Report the Commission recites its various objections to tax incentives. Perhaps the most serious of these is that tax incentives are viewed by the Commission as contravening its concept of equity. In Chapter VII of this submission, we will discuss the inordinate priority given by the Commission to its concept of equity. However, an indication of the Commission's philosophy on tax incentives is contained in the following quotation:

> "The great emphasis that has been placed throughout this Report on the paramount importance of horizontal equity and neutrality of tax treatment among different activities means that deviation from the full taxation of all income is only acceptable if there is an overwhelming reason for doing so".7/

6/ A study prepared for the Royal Commission by M. W. Bucovetsky, M.A., University of Toronto.

7/ Volume 4, Chapter 23, page 297.

The Commission elaborates its position concerning the depletion allowance and three-year tax exemption by stating that:

(a) they are costly in terms of tax revenue foregone;

(b) they are an inefficient means of stimulating exploration, since they "apply to the output that would have occurred without the incentive as well as to additional output"8/;

(c) "The depletion allowance provides a benefit only to established corporations with operating income"9/; and

(d) the present tax treatment induces "over investment" in the mining and petroleum industries which results in a "misallocation" of labour and capital to these industries and "reduced employment, investment and output elsewhere in the economy".

The Commission assumed that the tax incentives presently granted the extractive industries are unnecessary because foreign investment in these industries is, in its view, insensitive to after-tax rates of return and there is essentially no capital market bias against these industries. In so far as petroleum reserves are concerned, the Commission has further concluded that there is an over-capacity of conventional crude oil existing today and "limitless" reserves potential in the Athabasca Tar Sands and that there is "no obvious need for special incentives to encourage oil exploration".10/

These and other Commission views relative to the petroleum industry suggest a serious lack of understanding of the nature and complexity of industry operations. The following sections of this Chapter will attempt to define and place in proper perspective many factors which we feel require clarification.

Risk

The cursory treatment given the industry's argument regarding risk reflects a failure to grasp the real validity of the argument. The Commission acknowledges the difficulty in quantifying the degree of risk in any industry. Such a measure is particularly difficult to obtain for

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8/ Volume 4, Chapter 23, page 328.

9/ Volume 4, Chapter 23, page 329.

10/ Volume 4, Chapter 23, page 371.

the petroleum industry.

Although the Commission does acknowledge the fact that there is some element of unusual risk in exploratory operations, it relies upon industry-wide, successful well completion averages to support a conclusion that risk incurred by the individual enterprise is no greater than in the case of most other businesses. Unfortunately, well completion statistics give no indication of the <u>degree</u> of commercial success. In practice, the industry may record a well as being a successful oil or gas completion so long as the well will recover more than operating expenses. However, there is no guarantee that sunk capital expenditures may ever be fully recovered. More important is the fact that industry-wide averages do not measure separate company experience. Risk is borne by individual companies, not by the composite industry. Thus to use such statistics as a measure of the degree of uncertainty related to petroleum operations is misleading.

The unique risks facing the petroleum industry have been thoroughly documented in authoritative literature published both in Canada and the United States and in original submissions made by petroleum companies and associations to the Royal Commission on Taxation. We understand they will be re-stated in detail in briefs being submitted to the Minister of Finance. Thus, it seems unnecessary to dwell on the subject of risk in this brief other than to emphasize that risk in development, as well as exploratory operations, affects the industry's economics.

We find totally inadequate and misleading the Commission's (and Bucovetsky's) analysis and conclusions concerning relative risk of petroleum exploration and development as compared with other industries. The analogy between risk of the research activities of a small manufacturer and a small oil company is unrealistic. The petroleum industry is subject to greater risk than manufacturing as indicated by the fact that:

1. The Industrial Development Bank(established specifically to finance Canadian business which cannot find financing through conventional sources) will not finance exploration activities; but will finance small as well as large manufacturing and service businesses.
2. Chartered banks will provide production loans on proven properties only on a secured basis and will not finance exploration activities 'per se' but will finance manufacturing and service businesses.

In our view, these are just two of many illustrations which can be cited as proof that petroleum exploration is considered a high risk industry by the financial community.

Margin of Productive Capacity in Conventional Operations

The Commission is obviously concerned with presently unused productive capacity in the conventional crude oil industry. The Commission considers this unused capacity to be an inefficient use of financial resources and therefore attributes a social cost to it although there was no attempt by the Commission to quantify this cost. The Commission's analysis overlooked a number of important factors.

No industry or business can operate at 100 per cent capacity over the long-term for a variety of reasons including seasonal variations in demand, shut-downs, adverse weather conditions, changes in processes, etcetera. In this regard, the petroleum industry is no different from other industries.

Some margin of productive capacity is necessary to accommodate such factors as seasonal fluctuations in (and anticipated growth of) demand, variations in production practices, proper delineation and development of reservoirs, to secure new markets and to receive necessary funds for financing pipeline and other transporation facilities. In the case of Canadian natural gas, new markets and necessary financing for moving gas to these markets cannot be obtained unless the principals can demonstrate that at least twenty-years reserves are committed to such projects. Further, various government regulatory bodies will not permit the export of natural gas unless adequate reserves are available to meet thirty-year requirements of Canadian users. The long-range market outlook for Alberta oil and gas is encouraging. However, new markets will be captured only if the industry can clearly demonstrate to buyers and financial backers that adequate reserves are available. In other words, finding and development of reserves of necessity must precede production.

Because of the unpredictibility of exploration results (both in Canada and in competitive foreign areas serving the same markets as Canadian hydrocarbons), it is impossible to maintain the growth of indigenous reserves

close to probable demand. A margin of productive capacity is certainly preferable to under-capacity that would surely be brought on as a result of removing tax incentives which would make exploration in Canada relatively less attractive.

Athabasca Tar Sands

Insofar as petroleum reserves are concerned the Commission stated:[11/]

> "With the output of conventional crude oil substantially below 50 per cent of capacity, the Province of Alberta has been reluctant to grant permission to the industry to proceed with the exploitation of the tar sands on an adequate scale because this would entail a cut-back in the production of conventional crude . . . Hence, to grant increasingly generous tax concessions to encourage the discovery, at higher and higher costs, of more conventional oil when tar sands crude was available in limitless quantities but could not be exploited because of the limited market, would be perverse".

Elsewhere the Commission also argued that there is no obvious need for special incentives to encourage oil exploration by stating:[12/]

> "In particular, methods of extracting oil in commercial quantities from the almost inexhaustible Athabasca tar sands have been developed; the costs of discovering conventional crude oil are apparently rising; and the exploitation of the tar sands is being held back because of the limited market for oil. All of these factors suggest that there is no obvious need for special incentives to encourage oil exploration".

These statements and conclusions are a disturbing example of the Commission's lack of understanding of the petroleum industry and the inconsistency inherent in its analysis. These brief paragraphs, which are the primary basis for the Commission's recommendations for taxation of the petroleum industry, contain a number of statements which add up to unsubstantiated opinion and inaccurate, incomplete or inconclusive assumptions unsupported by objective evidence. We feel compelled and obligated to comment on these Commission remarks, because of:

(a) the incomplete explanation of our Tar Sands policy as being one "to avoid cut-back in the production of conventional crude";

(b) the inadequate understanding of costs of conventional versus Tar Sands oil;

(c) the misleading suggestion that Athabasca Tar Sands are available in limitless quantities;

11/ Volume 4, Chapter 23, page 326.

12/ Volume 4, Chapter 23, page 371.

(d) the reference to "the limited market" which did not explain the reasons for present market limitations and which also inferred that this is a static situation. In actual fact it is a dynamic situation which will change if Canada is in a position to supply additional hydrocarbons to export markets;

(e) the completely erroneous statement that <u>methods</u> of extracting oil in commercial quantities from the Tar Sands have been developed; and

(f) the failure to recognize that the present Great Canadian Oil Sands Limited (GCOS) development, which only commenced production on September 30, 1967, was considered to be economically feasible only because of the important tax incentives available - namely, depletion allowance, the three-year tax exemption for new mines and the timing of eligibility for capital cost allowance - the very same incentives which the Commission now proposes to eliminate.

Some enlargement of these points is in order, particularly because of the great importance attached to the Tar Sands reserves by the Commission.

The Commission's statement that "the Province of Alberta has been reluctant to grant permission to proceed with the exploration of the Tar Sands on an adequate scale because this would entail a cut back in the production of conventional crude oil", is a very superficial summary of an immensely complex subject. The Commission and its staff did not have the background necessary to realistically assess this subject, or in fact to make this statement.

It does not seem prudent policy to throw the Tar Sands wide open for development at a time when actual operations have not stood the test of time. Orderly development of the Tar Sands must be programmed. The objective of the Government of Alberta is to supplement but not displace conventional oil. The conventional oil industry has made cash expenditures in Western Canada totalling $10 billion since 1947, a substantial portion of which has been allocated to Federal, Provincial and Municipal Government treasuries. Consideration must be given to this substantial investment by the industry. To upset the present healthy condition of the petroleum industry by the undue urging of Tar Sands development, which could prove to be uneconomic, would be irresponsible. However, the need to maintain a leading position in technological development of Tar Sands over the U.S. oil shales is one of the prime reasons for permitting Tar Sands development at this time. We believe Tar Sands production should be integrated into the overall hydro-

carbon supply at an appropriate rather than a disrupting rate.

Many years may be required to establish the magnitude of economically recoverable reserves from the Tar Sands and the costs of production vis-a-vis conventional oil. The richness and accessibility of Tar Sands reserves are not consistent throughout the reservoir. They vary considerably in terms of richness of oil content, accessibility and thickness. The GCOS operation involves development of a relatively high grade portion of Tar Sands reserves situated at a depth with very little overburden. Moreover, development of less rich reserves that are situated at greater depths will be faced with rapidly increasing cost curves under present Tar Sands technology. In other words, the race will be between technology and a rising real cost curve.

Mining processes, such as GCOS, are probably only applicable to some 10 per cent of the reserves located in the Athabasca area. No process for "in-situ" recovery methods suitable for recovery of the remaining reserves has yet been approved for commercial development. Bucovetsky's reference that there are no technical obstacles to be overcome is in error. None of the currently contemplated methods of recovery of synthetic oil are fully proven as yet.

This raises a question concerning the validity of the Commission's statement that "if the tar sands are not now competitive with conventional crude, they will be competitive in the near future". There is no basis in fact for this statement (for the reasons cited earlier) nor for the deductive reasoning that as a result, Canada's reserves "will be limitless".

The economic operation of a Tar Sands plant requires maintenance of a reasonably constant long-run throughput at close to capacity. This builds a degree of inflexibility into the supply pattern. Conventional oil reserves offer flexibility to accommodate sudden increases in domestic or export demands caused by international crises, etcetera, which could not be met as easily under Tar Sands production capabilities. If the Tar Sands were to be the prime source, over-capacity would have to be provided. In such an event economic feasibility of the GCOS project would have been reduced in relation to the margin of additional capacity required.

The Commission's reference to a limited market for oil is an over simplification of fact. Markets for crude oil and natural gas do not follow the same development pattern common to many manufactured products. Forty per cent of Canadian oil production is exported to the U.S. The level of these exports is governed by the Oil Import Program of the United States Department of the Interior. The long-range prospects for additional Canadian exports to the U.S. appear encouraging, but they are in no way guaranteed. One factor which will influence U.S. regulatory authorities to increase imports of Canadian oil and gas - particularly gas - will be the long-range assurance of adequate Canadian supplies.

Perhaps the most irrational aspect of the Commission's analysis of Tar Sands development is the failure to consider the fact that economic development of the GCOS scheme and future Tar Sands operations requires the three major tax incentives presently available, namely: depletion allowance, the three-year exemption of mines from tax payments and the timing of eligibility for capital cost allowances - yet these incentives which are essential to Tar Sands development will all be removed under the Commission's recommendations. This means that implementation of the Commission's recommendations would make both conventional exploration and development and Tar Sands development economically infeasible. Should such development be retarded, a serious crude oil supply deficiency could develop very quickly. Assuming the recent historical growth rate in demand continues into the future, existing supply would last about fourteen years.

A further major oversight by the Commission relates to natural gas. Although a minor amount of natural gas is produced under the GCOS process, it is utilized in the refining process. It presently appears that GCOS will have to purchase natural gas in order to meet its total energy needs. Thus, without conventional oil exploration, additions to natural gas reserves would be eliminated since many natural gas discoveries result from the search for crude oil. The implications of such a development are most serious. Long-range supplies for domestic markets would be threatened and Canadians would be deprived of the opportunity to capitalize on growing U.S. markets. Increased gas exports have an obvious advantage in terms of increased contributions to balance-of-payments. Present payments are in the order of an impressive $100 million per year.

Prorationing

As indicated earlier, the Commission's Report drew heavily on Bucovetsky's study. Presumably the Commission was influenced not only by Bucovetsky's points to which the Report specifically refers but also by other points contained in his analysis. For these reasons, we feel it is necessary to demonstrate where Bucovetsky's analysis is superficial or wrong - as in his treatment of the subject of prorationing, which he erroneously describes as a "compulsory cartel".

A cartel is defined as:

> "a voluntary combination of independent private enterprises supplying like commodities or services that agree to limit their competitive activities by allocating customers or markets, regulating quantity or quality of output, pooling returns or profits, fixing prices or terms of sale, exchanging techniques, trademarks or patents or by other methods of controlling production, price or distribution".13/

Because the proration system in Alberta is compulsory, not voluntary, it cannot be considered a cartel. Prorationing pertains solely to production and not marketing. Under the system there is no contract between companies to co-operate in regulating production. Prices are not controlled by the Alberta Government, the Oil & Gas Conservation Board, or by industry-government collusion. Prorationing was instituted in Alberta in 1951 following a rapid series of discoveries and development, under the land tenure system, of oil pools in the Province. The immediate reason for prorationing was that varying rates of withdrawal within pools were depriving some mineral owners of an opportunity to recover their minerals.

Prorationing is more complex than indicated by Bucovetsky's description. Under conditions where productive capacity exceeds market demand, the absence of prorationing, at least within pools, could remove the opportunity for mineral owners to recover and market their minerals and could result in the development of reservoir conditions leading to waste. Both of these situations would be contrary to modern conservation concepts.

13/ Source: Dictionary, Edmonton Public Library.

Bucovetsky acknowledged these points in his statement:

> "But if property rights to a mineral body are not exclusive to one decision-making unit, a much stronger case may be made for a conservationist policy. Oil and gas deposits are non-specific in this sense. Property rights are subject to the "rule of capture", under which whatever one holder of mineral rights can withdraw from the migratory underground pool is his to take and keep. Furthermore, ultimate total recovery of petroleum depends on adequate maintenance of gas pressure and the rate of flow of the liquid crude. Under these circumstances, it is in the self-interest of each producer to attempt to bring to the surface as much crude oil as he can, as quickly as possible, before his neighbour does the same. In the absence of public intervention or monopoly control, one could expect a more rapid rate of depletion and a lower ultimate recovery than would be socially desirable, as well as a waste of economic resources in the creation of excessive exploitive capacity". 14/

The intention of prorationing is therefore the direct opposite to the intention of cartel. It is required by the public interest for the reasons outlined by Bucovetsky. There is no attempt to limit competition through prorationing. Bucovetsky fails to recognize the nature of markets for Canadian oil as described under the Tar Sands discussion above. Because of the National Oil Policy and the U.S. Oil Import Program, an elimination of prorationing in Alberta would not result in a change in demand for Canadian crude oil.

As explained in A White Paper on Human Resources Development:

> "The operations of the Alberta Oil and Gas Conservation Board have contributed to productivity by requiring orderly and efficient development of petroleum resources, and by developing an effective conservation program designed to assure the maximum ultimate recovery". 15/

Allocation of Resources

The following statement from the Report indicates the Commission's view that present tax incentives have diverted an anomalous flow of capital into the extractive industries:

14/ M. W. Bucovetsky, The Taxation of Mineral Industries, "Studies of the Royal Commission on Taxation, No. 8", page 76.

15/ A White Paper on Human Resources Development, Government of Alberta, page 76.

"It is true that in the absence of these concessions the income generated by mining and petroleum almost certainly would have been less, but the increased investment in other industries of funds which were invested in mining and petroleum would have increased taxable revenues from these other industries".16/

The Commission evidently believes any reduced flow of capital into the extractive industries, brought about by removal of certain tax incentives, will be diverted into other Canadian industries. This is an incorrect conclusion supporting suggested changes in existing tax policy that would have serious adverse effects for Canada and more particularly for Alberta and its citizens.

At the end of 1963 non-resident owned capital amounted to $4.7 billion out of total capital employed in the petroleum industry of $7.3 billion.17/ This foreign capital would not have been employed in other Canadian industries. Rather it would have been diverted to investment in the petroleum industry in other parts of the world. The Commission failed to recognize that investors have a choice as to where to place their investment capital. Certainly, capital invested in the Alberta petroleum industry would not have been attracted to other Alberta manufacturing since a major portion of our manufacturing activity has been developed to serve the petroleum industry.

In addition, the Commission failed to identify the other Canadian industries into which these funds would have been channelled. It seems unlikely that the Canadian manufacturing industry, for example, could have supported an additional $7.3 billion investment particularly when foreign investors had other more attractive investment alternatives outside Canada.

The reason for foreign capital being attracted to Canada's petroleum industry has been the existence of tax incentives which help offset:

16/ Volume 4, Chapter 23, page 297.

17/ Dominion Bureau of Statistics Quarterly Estimates of Canadian Balance of International Payments, 1966.

(a) the element of risk unique to the petroleum industry; and

(b) the unusual time delay between the exploration for and development of reserves and the marketing of production.

It has only been the existence of tax incentives counterbalancing these economic hazards and disadvantages that has enabled Canadian reserves to be developed ahead of demand.

Apart from the need for a cushion in capacity to develop new markets, the disadvantage of not having such a cushion in times of national emergency became apparent to the Canadian Government during World War II.

Therefore, we believe tax incentives which have attracted large sums of capital to Canada's petroleum industry can be fully justified from both an economic and a national security standpoint. In this light, it is virtually impossible to rationalize the Commission's contention that there has been a misallocation of resources.

In addition, the Commission's belief that the removal of tax incentives will divert capital into other industries fails to recognize the specialized nature of this capital. It is capital primarily backed by technical skills oriented to the search for hydrocarbon resources. Removal of the incentive to continue this search in Canada will cause the capital to flow into similar projects outside our country.

The Commission further assumes that, under conditions of full employment, investment in petroleum (and mining) diverted a portion of the labour force to these resouce industries. In our opinion, all regions of Canada have not enjoyed full employment during the postwar period. Certainly, as pointed out in Chapter II, Alberta would have had a serious unemployment problem subsequent to 1946 if employment in oil had not picked up the slack resulting from rapid mechanization of agriculture in Western Canada.

The Economic Council of Canada has warned of the difficulty ahead in maintaining full employment. In dealing with policy implications, the Council stated in its latest report, released September 1967, that:

> "Recent developments within the Canadian economy provide no cause for complacency. Although a huge expansion of output and employment has been achieved in the 1960's, and although the unsustainable rate of overall economic expansion over the first half of the decade has moderated without a major rise in unemployment, a very high rate of both output and employment must be sustained for many years to come if Canada's basic economic goals are to be realized".18/

In view of this prospect, reasonable incentives must be provided to attract capital to invest in future development of Canadian resources, particularly in provinces like Alberta where it will be impossible to achieve long-range economic objectives without the stimulating effect of a healthy petroleum industry.

Those responsible for establishing policies which will influence foreign investment in Canada should never lose sight of the fact that there is a world-wide shortage of investment capital. To discourage its entry into Canada will be to defer or completely forego potential economic growth and development.

In its analysis of allocation of resources, the Commission apparently restricted its consideration to corporate income tax payments and seems unduly concerned with the belief that corporate taxes paid by the petroleum industry may be relatively lower than those paid by some other industries. However, the Commission made a serious omission by not considering the overall direct tax burden of the petroleum industry in terms of all forms of tax revenue paid to municipal, provincial and federal governments. Further, it ignored the multiplier effect of the petroleum industry in terms of taxes paid by oil industry employees, its suppliers, their employees and employees of various government agencies which are partially or wholly concerned with petroleum industry matters.

18/ The Canadian Economy from the 1960's to the 1970's, Fourth Annual Review: Economic Council of Canada, September 1967.

Insensitivity to After-Tax Rate of Return and the Effect of Commission Recommendations on Investment Decisions

The Commission makes the astonishing statement that petroleum investment is insensitive to after-tax rates of return. The Commission's basis for this position is in direct conflict with public statements made by a number of companies - both within and outside the petroleum industry.

The Commission does acknowledge that:

> "It is difficult to make precise estimates of the overall effects of our proposals on the after-tax rate of return from mining and petroleum companies".19/

Thus the confusion in the minds of the Commission is self-apparent.

Subsidies

The Commission recommended that subsidies would be a better form of incentive to oil companies than those presently available.

We basically disagree with the concept of subsidies where other more efficient alternatives do exist. Fundamental to this disagreement is the belief that subsidies encourage inefficient investment. Tax incentive benefits accrue primarily to successful, efficient business ventures.

It is true that there is a "cost" to the government of such incentives to the extent that tax revenue is foregone. However, the Province of Alberta remains strongly convinced that this "cost" is more than offset by the many economic benefits accruing from the incremental investment induced by the existence of tax incentives.

The uncertainty implicit in the granting of government subsidies, would undoubtedly have an unsettling effect on business investment confidence. Business would naturally need to know how much subsidy assistance would be available, when it would be available and the length of time for which such assistance could be anticipated. Reasonable long-term assurances would be paramount to stabilizing business confidence, but such assurance would probably not be available from appropriate government authorities.

In our view subsidies generally tend to create an artificial economic climate. We regard the granting of special subsidies as expediency

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19/ Volume 4, Chapter 23

which ignores the realities of economics and geography and distorts sound resources development.

Other Considerations

The effect of reduced investment by the petroleum industry on Canada's international balance of payments may not be immediate. The reason for this is that the industry would likely continue to produce its presently developed inventory at pre-Commission projected rates for a while. However, by lowering investment, the industry will fail to develop new supply at the rate that might otherwise have been achieved. To this extent, it will be unable to fully supply the potential longer-term demand. Because exports comprise a large portion of industry sales, the relative effect on Canada's international balance of payments will be adverse.

Another factor inadequately considered by the Commission is the contribution made by the petroleum industry towards upgrading the quality of Alberta's labour force. As previously mentioned, the industry requires a high degree of technical and management proficiency. However, many of the skills are specialized. Should employment opportunities for personnel with these skills diminish, as they most certainly would upon implementation of the Commission's proposals, the result will be the emigration of a highly qualified segment of Alberta's labour force.

Despite the Commission's expectation that its proposed system would merely convert foreign direct investment from equity to debt capital, we are not convinced the proposed system would achieve this result. In many instances, capital is invested in a young country such as Canada for the expressed purpose and with the hope of obtaining a higher return than that offered by interest on debt. In other words, the foreign investor is willing to assume a higher degree of risk in order to participate in higher potential gains. The Province of Alberta has materially benefited from a high degree of foreign investment. Development of the Province's hydrocarbon resources has taken place at a much faster rate than would have otherwise been possible. Consequently, the Government of Alberta is deeply concerned over prospective changes in tax legislation that would greatly retard the flow of investment capital into the Province. The impact of this retardation on the Province's economy would be most serious.

Chapter VI

IMPLICATIONS OF COMMISSION RECOMMENDATIONS ON FEDERAL-PROVINCIAL FISCAL RELATIONS AND ALBERTA'S FISCAL CAPACITY

This Chapter begins with a discussion of the Commission's apparent philosophy and resulting recommendations in the area of federal-provincial fiscal relations. The Government of Alberta's reaction to this philosophy and recommendations is noted followed by a quantitative analysis of the potential impact of the Commission's recommendations for the petroleum industry on the Government of Alberta's fiscal capacity.

Strengthening of federal-provincial fiscal co-operation was one of the main objectives of the Commission. Despite this stated objective, the Commission seemed to devote most of its comments towards substantiating its views of the need for greater centralized fiscal authority. The Commission apparently was concerned that the senior level of government presently has inadequate powers to direct the stability and growth of Canada's national economy, and to achieve adequate control over the distribution of the nation's resource wealth.

The Commission recommended[1/] that the provinces should:

1. abandon the corporate tax field to the exclusive use of the federal government;

2. abandon succession duties;

3. accept a common federal-provincial base for income and sales taxes;

4. establish an upper limit on the provincial governments' share of personal income tax (i.e., the federal government should maintain its present share of the personal income tax and strongly resist further provincial abatements);

5. establish a joint federal-provincial retail sales tax that would replace the existing manufacturers sales tax and the present provincial retail sales tax. (The latter is not presently applicable in the Province of Alberta);

1/ Volume 1, Introduction.
Volume 2, Chapters 1 and 3.
Volume 6, Chapter 38.

6. exercise restraint in provincial government expenditures during periods of inflation;

7. deposit the difference between the tax revenue that:

   (a) is received from the province's share of income tax and retail sales tax during periods of inflation, and

   (b) would be theoretically received from these sources under conditions of full employment and no inflation; and

8. agree to intensify federal-provincial consultation on stabilization policies and eventually become committed to a binding federal-provincial agreement on stabilization.

The Commission's recommendation for integration of personal and corporate income would also strengthen federal fiscal power at the expense of the provinces. The anticipated effect of integration will be to increase personal income. However, as cited above, the Commission proposes to restrict provincial government access to this source of tax revenue. Therefore, any revenue increases from this tax source would accrue primarily to the benefit of the federal government.

The Government of Alberta is greatly disturbed, not only by many of these recommendations, but, by the underlying philosophy upon which they were based. The loss of provincial autonomy implicit in the Commission's recommendations would seriously impair the provincial governments' ability to carry out their constitutional responsibilities in the fields of education, health and social welfare, highway development, etcetera.

We believe the Commission placed undue emphasis on the effectiveness of fiscal policy in guiding Canada's economic destiny. Fiscal policy, while an important integral part of the many forces which influence economic growth, is not necessarily the dominating force. International economic conditions plus national monetary and commercial policies also strongly influence our country's development.

In our opinion, the most important factor affecting Canada's economic stability lies beyond her direct control. Specifically, our heavy commitment to international trade inevitably makes this nation's

economy more vulnerable to fluctuations in world economic conditions than countries with better-balanced, more diversified internal economies. Canada's economic stability is particularly influenced by prevailing conditions in the U.S., our major trading partner. The Economic Council of Canada does not consider this influence undesirable as reflected by its comment that:

> "Canada's continued interdependence with the world economy will in fact help to promote the development of a more mature and advanced, and a more enterprising and forward-looking economy over the years ahead."2/

The opportunities for long-term growth and development provided by active participation in the dynamic world economy far outweigh the limited advantages that may be obtained as a result of the excessive concentration on stabilization policy measures recommended by the Commission. Although the Commission did not discuss Canada's commercial policy as such, it must be recognized that the nation's commitment in this area diminishes the effectiveness of fiscal policy in controlling our economic growth.

Another important factor affecting economic growth, but not evaluated by the Commission, was monetary policy. Canada's exchange rate relative to other world currencies and Canada's domestic interest rates on securities will have a direct bearing on the balance of this country's import versus export trade, the attraction of foreign investment and the availability of domestic capital. The ability to trade and to obtain capital for domestic investment purposes also strongly influences economic growth. The combined importance of international economic conditions and national commercial and monetary policies suggests that the Commission over-stressed the role played by fiscal policy.

The Commission's approach to federal-provincial fiscal relations failed to adequately consider the existence of regional economic imbalances, many of which are unalterable. These imbalances are reflected

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2/ Economic Council of Canada, First Annual Review, December 1964.

in:

(a) differences in financial, human and natural resources;

(b) density of population and rate of population growth;

(c) ratio of unemployment to population;

(d) degree of urbanization and industrial development;

(e) price differentials for commodities consumed; and

(f) competitive position of commodities produced (i.e., as determined by proximity to markets, transportation problems, cost of production, etcetera).

The Commission seemed to put undue emphasis on centralizing fiscal policy as the only means of stabilizing economic growth. In our opinion, centralization of fiscal policy, in itself, will not assure economic growth, particularly since our overall economy is tied to international developments.

In referring to the administration of federal policies and programs that will have a bearing on regional economic development, the Economic Council of Canada stated that "a high degree of departmental centralization and decision making may be inappropriate in adopting federal programs to the particular needs of widely diverse regions."[3] This indicates Council's recognition of a need for sensitivity to the particular regional situation.

Provincial governments are more conversant with their respective regional needs than federal agencies. In order to properly perform their regional responsibilities, provincial governments must maintain a reasonable degree of autonomy and have adequate fiscal capacity.

Diversified expenditures and sources of revenues for federal, provincial and municipal governments in Canada make it exceedingly difficult to balance regional disparities. Consequently, it is imperative to maintain fiscal capacity and jurisdictional authority for each

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3/ Economic Council of Canada, Third Annual Review, November 1966, page 266.

level of government commensurate with their respective responsibilities.

The federal government should only have those powers necessary for the provision of those functions falling within the area of its responsibilities.

Beyond adequate provision for those functions under federal government responsibilities, we believe the growth and development of Canada's national economy can be achieved most effectively through strengthening the individual regions of the country. It will not be achieved through emasculating the economic strength and fiscal capacity of the provinces.

In summary, the Commission failed to:

(a) evaluate the <u>relative</u> importance of fiscal policy as a means of stabilizing and encouraging economic growth;

(b) give due consideration to regional imbalances; and

(c) recognize the constitutional division of responsibility amongst the various levels of government.

Consequently, the Government of Alberta concludes the Commission's philosophy of centralizing fiscal authority will add to the problems confronting Canada's existing federal state.

1. <u>General Economic and Administrative Implications</u>

The Commission argues that centralized control over discretionary policy has the advantage of being more directly and immediately effective in counteracting weakening conditions in the economy. The Commission concludes that this consideration supports its contention that an increase in the provincial share of personal income tax is undesirable. The Commission further argues that stabilization policy should take precedence over other considerations.

The Commission attached considerable importance to its concern over "revenue drag." Basically, revenue drag refers to the situation where progressive taxation tends to generate government revenue at a rate exceeding the growth of the Gross National Product in an inflationary economy.

To offset this drag the Commission suggests the following alternatives:

1. increased federal expenditures

   (a) on goods and services,
   (b) on transfer payments to persons, or
   (c) on transfer payments to provinces; and

2. reduced federal taxes.

Although the Commission tends to dismiss the latter alternative, it does not firmly commit itself to any specific recommendation in this area.

The Commission espouses the concept of "potential GNP" which it defines as the potential output under conditions of virtually full employment of capital and labor. The Commission proposes that potential GNP should be the nation's economic objective with discretionary stabilization policies directed at maintaining the actual GNP as close to the potential GNP as possible. The Government of Alberta would support the broad objective of this concept provided adequate consideration is given to regional growth.

The Commission's concern over revenue drag may be somewhat exaggerated in view of Canada's economic experience in years subsequent to those analyzed by the Commission. Although the Canadian economy has generally experienced inflationary conditions and essentially full employment, government expenditures have been rising at a faster rate than government revenues. Thus, the "drag" has not materialized. In fact, the concern may be just the reverse, particularly at the provincial and municipal levels.

Any future changes in government policies and regulations should be directed at achieving an objective balance between economic growth and the expenditure programs required by various levels of government to fulfill their responsibilities.

Consideration must also be given to the degree of taxation that can realistically be imposed without significantly inhibiting economic growth. We may be dangerously near this level now. If this is so, the alternative becomes one of establishing priorities for government

expenditures. In addition to striving for a more effective programming of government revenues and expenditures, an efficient system of revenue collection is also desirable. The Government of Alberta agrees that unnecessary duplication of various government facilities for the purpose of revenue collection is undesirable. The collection by the federal government of both the federal and provincial government shares of personal income taxes is a practical example of efficiency already achieved in the current system. We believe that further administrative efficiencies of this type may be possible once some of the longer term objectives of the tax system have been resolved.

2. Adverse Affect Upon The Government of Alberta's Future Fiscal Position

The Commission sets forth recommendations that will seriously affect the petroleum industry, hitherto an important source of revenue for the Government of Alberta. The industry contributes revenue in many forms both direct and indirect. Briefly these include: bonus prices, acreage rentals, royalties and non-income taxes plus personal and corporate income taxes. Revenue cutbacks by the petroleum industry as a result of Commission recommendations will commensurately reduce Alberta Government revenues. This is but one area of reduced revenue the Province can anticipate should the Commission's recommendations be adopted. The Commission's proposal to restrict the access of provincial governments to personal income taxes and to abandon the corporate tax field will further impair fiscal capacity of governments at the provincial level.

The Government of Alberta is deeply concerned over the outlook for its future revenues in relation to anticipated expenditures, should certain of the Commission's recommendations be adopted. Until the fiscal year ending March 31, 1966, Alberta's revenues exceeded expenditures. For the fiscal year ending March 31, 1967, a negative balance of $82 million was recorded and a further deficit of $67 million is estimated for the current fiscal year. Without increases in revenue from existing revenue sources, access to new sources of revenue or reduced expenditure programs (or some

combination of these) the situation will worsen. Implementation of various Commission recommendations will reduce the fiscal capacity of the Government of Alberta and as a result, will further aggravate this serious problem.

The historical pattern of provincial-municipal revenues and expenditures clearly shows that revenues are relatively sensitive to changes in economic activity whereas expenditures are relatively insensitive.[4/] The demand on provincial-municipal governments for such capital projects as schools, hospitals, highways and universities has reached the point where they are virtually considered "non-discretionary" by the public.[5/] In other words, it becomes increasingly difficult to postpone such projects regardless of prevailing economic conditions.

Nearly 70 per cent of Alberta's net revenue comes from two major sources:

(a) direct revenues received from the petroleum industry; and

(b) corporate and personal income taxes.

Both would be adversely affected by the Commission's recommendations.

The remaining 30 per cent is derived from pari-mutual tax, gasoline and fuel taxes, etcetera; operation of the Alberta Liquor Control Board; privileges, licences and permits; business and estate taxes; plus other non-direct tax sources. Total revenue from this group is reasonably predictable from historical trends.

The comprehensive tax base recommended by the Commission would effectively eliminate estate taxes as they exist under the present tax

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4/ "The Bases and Effects of Provincial-Municipal Fiscal Decisions" by A. W. Johnson, Assistant Deputy Minister, Department of Finance and J. M. Andrews, Bank of Canada.

5/ National Industrial Conference Board, Inc. - The Conference Board Record - "Provincial and Municipal Governments: Some Problems in Budget Balancing", April 1967.

system. However, the inclusion of capital gains, gifts and bequests in taxable income at full rates would more than offset any potential advantage that an individual might realize from the elimination of estate taxes. (This point is discussed in greater detail in Chapter VII).

The Government of Alberta recently passed legislation that would enable it to rebate the Province's 75 per cent share of federal estates taxes to Alberta residents under certain conditions. We believe this form of tax relief is a desirable means of encouraging domestic capital to remain in Alberta rather than flee to tax havens outside Canada. The same principle could be introduced on a national scale. In our opinion, a tax system that creates investment incentive and capital retention will, undoubtedly, be an effective means of fostering economic growth and development in Canada. If a satisfactory investment climate is created, we believe estate capital will be re-invested in Canada. The long-term economic benefits extending from this re-investment will greatly outweigh immediate benefits to government in terms of revenues from estate taxes.

In summary, the Government of Alberta supports the Commission's proposed elimination of estate taxes but would resist offsetting recommendations.

(a) Direct Revenues Received from the Petroleum Industry

Direct revenues received from the petroleum industry in the form of royalties on production, crown reserve purchases and land rentals currently amount to roughly 50 per cent of the Province's total net revenue.

Barring changes that might adversely affect the long-term stability-of-supply outlook for Canadian oil and gas, Alberta royalty revenues (conservatively-estimated) should continue to grow at historical rates from $76 million in 1967 to $110 million in 1970 and $190 million in 1975.[6/]

6/ Calculations have been made assuming the continuation of prevailing tax policy (Table VII-1) and assuming implementation of the Commission's recommendations (Table VII-2).

Land rental and crown sale revenues, on the other hand, are a more direct function of the industry's exploration and development activity.[7/] Also, revenues from these sources are normally more erratic and relate to land availability and geological opportunity. Petroleum industry activity may begin to level off in Alberta during the 1970's as the number of such opportunities diminishes. Therefore, Government of Alberta revenues from these sources would not continue to rise at historic rates of growth.

However, total petroleum industry contributions to the Provincial Treasury should still be substantial through 1975. In the composite, direct petroleum industry contributions could rise from $238 million in 1967 to $320 million in 1970 and $465 million in 1975.

Because of Government of Alberta regulations regarding acquisition of rights to crown reserves, crown reserve purchases are one cost component over which the industry can exercise some control. To the extent possible, the industry would inevitably attempt to cushion the impact of lost depletion allowance and a change in acquisition cost write-off provisions by reducing bid prices for crown acreage. The resulting impact on Government of Alberta revenues would be immediate and direct.

Even if the depletion allowance is not removed, Government of Alberta crown sale revenues could still be substantially reduced by the proposed change in acquisition cost write-off provisions. Under present regulations, such purchases may be written off immediately. If the petroleum industry should be required to amortize such purchases on a unit-of-production basis, the inevitable result would be lower bonus prices paid to the Government of Alberta.

7/ Rental and crown sales revenue were projected to increase through 1970 at historic growth rates with some modification in the rates thereafter.

Table VI-1 shows net general revenues under existing tax regulations for the fiscal year 1967, 1970 and 1975. Table VI-2 shows the potential impact of Commission recommendations on future Alberta Government revenues from the petroleum industry. Although it is difficult to precisely estimate the impact of Commission recommendations on future industry investment, reductions in crown reserve purchases in the 20 per cent to 50 per cent range are not considered outside the realm of possibility. Rentals might not be quite so severely affected but would still drop as companies would reduce acreage holdings. Investment cutbacks would automatically reduce future reserve additions and, therefore, long-term production rates and Government of Alberta royalty revenues based on production.

The composite effect of industry cutbacks could reduce Alberta Government revenues from the petroleum industry by $40 to $80 million in 1970 and $75 to $150 million by 1975. Reductions of such magnitude are obviously viewed with great concern by the Government of Alberta. The Provincial Government's fiscal capacity would be severely impaired by these potential losses in future revenue.

(b) Personal and Corporate Income Taxes and Retail Sales Taxes

In the decade 1956 to 1966, personal income taxes payable in Canada rose at the average annual growth rate of over 11 per cent or approximately the same rate as total provincial-municipal government expenditures.

Canadian corporate taxes payable, after appearing to plateau in the mid-1950's, have shown an average annual growth of nearly 6 per cent in the 1960's as a result of the nation's economic upsurge during that period.

Assuming these growth rates continue into the future, Alberta's existing share of personal and corporate income taxes would grow from a 1967 level of $110 million to $145 million in 1970 and $230 million in 1975.

If Commission recommendations regarding provincial government sources of tax revenue are followed, the provinces would have:

(a) no further percentage access to the personal income tax field;

(b) to abandon the cororate tax field;

(c) to resort to a retail sales tax as a revenue alternative; and/or

(d) reduce future expenditures.

Loss of the corporate income tax would mean the Government of Alberta would forego projected revenue amounting to $40 million in 1970 and $55 million in 1975.

The Commission's suggested retail sales tax would be an inadequate substitute for the loss of corporate income tax revenue plus restricted provincial government access to the faster growing personal income tax yield.

3. Summary

The Commission, in setting forth its philosophy of centralized fiscal authority, failed to adequately consider several very relevant factors. The most important of these factors are:

(a) fiscal policy is not the only factor influencing stability in Canada's economic growth; and

(b) a reasonable degree of provincial government fiscal capacity and autonomy must be maintained in order for the Government of Alberta to satisfactorily carry out its constitutional responsibilities.

The Commission's preoccupation with centralized fiscal authority casued it to give inadequate consideration to the regional implications of its recommendations. The Government of Alberta strongly contends that provincial government understanding of regional problems makes it imperative that provincial autonomy be preserved. However, we are not unmindful of certain common objectives of the federal and provincial governments. Consequently, we would support continuing efforts to bring federal and provincial objectives into reasonable balance with one another.

Alberta's fiscal outlook, under existing tax regulations and existing federal-provincial transfer payment arrangements, will require intensive analysis to resolve a potentially mounting deficit problem. The Commission's recommendations that will:

(a) adversely affect the petroleum industry and, consequently, provincial government revenues accruing therefrom;

(b) restrict provincial government access to personal income tax revenue; and

(c) cause the provinces to abandon the corporate tax field

are viewed with great concern by the Government of Alberta. The combined effect of these recommendations will more than offset any potential advantages envisioned by the Commission from a provincial retail sales tax.

Table VI - 1

NET GENERAL REVENUES

Government of Alberta

PROJECTIONS UNDER EXISTING TAX REGULATIONS

NET GENERAL REVENUE[1/]	Millions of Dollars 1967[2/]	1970	1975
Taxes on Income			
Personal	76.6	105	175
Corporate	33.0	40	55
Total	109.6	145	230
Taxes on Consumption[3/]	52.5	65	95
Taxes on Assets			
Business	3.8	5	5
Estate 4/	5.0	-	-
Total	8.8	5	5
TOTAL TAXES	170.9	215	330
Privileges, Licences & Permits[5/]	37.8	45	55
Petroleum & Natural Gas Revenues			
Crown Reserve Sales	110.0	135	175
Royalties	76.0	110	190
Fees and Rentals	52.0	75	100
Total	238.0	320	465
Government of Canada	6.4	*	*
Alberta Liquor Control Board	37.1	50	70
Other	13.1	20	25
TOTAL	503.3	650	945

Note: Projected data are rounded to the nearest $5 million.

1/ Does not include Federal Government financial assistance.

2/ Estimated by the Provincial Treasury Department, Government of Alberta for fiscal year ending March 31, 1968.

3/ Includes taxes on gasoline and fuel consumption plus pari-mutual taxes.

4/ Government of Alberta's share of the total estate tax.

5/ Excludes petroleum and natural gas revenues.

* Not projected.

Source: Government of Alberta.

Table VI - 2

IMPACT OF COMMISSION RECOMMENDATIONS ON REVENUES FROM THE PETROLEUM INDUSTRY

Government of Alberta

	1970		1975	
	Per Cent Reduction	$ MM	Per Cent Reduction	$ MM
Under Existing Regulations				
Total Revenue 1/	n.a.	650	n.a.	945
Reductions in Direct Revenue Received from the Petroleum Industry				
(1) Minimum Effect				
Crown Reserve Sales	20	30	20	35
Fees and Rentals	10	10	20	20
Royalties	-	-	10	20
Total		40		75
(2) Possible Effect				
Crown Reserve Sales	50	70	50	90
Fees and Rentals	15	10	30	30
Royalties	-	-	15	30
Total		80		150

Note: Effect rounded to the nearest $5 million.

n.a. - not applicable.

1/ Excludes Federal Government assistance.

Source: Government of Alberta.

Chapter VII

A REVIEW OF COMMISSION PHILOSOPHY AND MAJOR RECOMMENDATIONS

Introduction

This Chapter begins with a discussion of alternative objectives of a tax system as set out by the Commission. A system can be designed primarily to (i) maximize economic growth or (ii) to maximize immediate equity. This discussion is followed by a review of the Commission's proposed comprehensive tax base and its recommendations for introducing an untested taxation system. Particular emphasis is given to those recommendations in which there seem to be fundamental differences between our views and those of the Commission. The impact of Commission recommendations on agriculture and petroleum is discussed in Chapters IV and V respectively.

Frequent reference is made in the following discussion to A White Paper on Human Resources Development which was released by the Government of Alberta in March 1967. These references are made to illustrate obvious differences between our economic and political philosophy and that reflected in the Commission's Report.

1. Conflicting Objectives of the Tax System

The Commission recognized that "The tax system that provides maximum encouragement to economic growth will differ in general from the tax system that maximizes equity, so that there must be an ultimate trade-off between growth and equity".[1/]

1/ Report of the Royal Commission on Taxation, Volume 2, page 43.

The Commission recommends tax measures that redistribute income in favour of those at the bottom of the income scale even if this will necessitate some sacrifice of future growth.[2/]

The Commission assigned highest priority to the object of equity, stating that "our task requires us to make recommendations that would lead to an equitable distribution of the burden of taxation. Thus, the need for an equitable tax system has been our major concern and has guided us in all our deliberations."[3/]

An underlying problem is the fact that it is virtually impossible to define "equity" in a manner acceptable to all. The Commission states that, a tax, if it is to be imposed equitably, should provide for (i) horizontal equity (the equal tax treatment of persons in the same circumstances, that is, with similar claims on resources), and (ii) vertical equity, a "fair" allocation of the total tax burden between those in different circumstances.[4/]

To others, equity means avoidance of taxation of unequals at identical rates, so as to give equal incentives to those who are prepared to make investments in high-risk ventures, or recognition of those who are frugal and who build a capital base through prudent investments.

The Commission strongly favours the ability-to-pay approach to apportion the burden of taxation. This approach takes the position that taxes are equitable when they are levied according to a defined capacity, or ability to pay, of individuals or groups.[5/]

In referring to the importance it places on the redistributive function of the fiscal system, the Commission stated that the adoption of a tax system that would subject a base that measures the economic power of each tax unit to a schedule of progressive marginal rates would ensure that

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2/ Volume 2, page 239.

3/ Volume 2, page 17.

4/ Volume 3, page 331.

5/ Volume 3, page 3.

the costs of government transfers and expenditures were allocated among Canadians in proportion of their abilities to pay. Such a tax system, according to the Commission, when combined with a progressive transfer-expenditure system that provided relatively greater benefits to low income families and individuals, would achieve the following results:

(a) low income families and individuals would become net beneficiaries of government;

(b) middle and upper income families and individuals would become net contributors to government;

(c) the lower the income of the family or individual the greater the relative net benefit obtained from government.6/

Although we agree with the Commission's subsequent suggestion that society is committed to providing equality of opportunity and improving the well-being of those who have the least economic power, we feel that this can best be achieved by attempting to maximize economic growth in Canada rather than attempting to maximize equity and redistribution of wealth through the taxation system.

Without maximum economic growth in the next decade it may be difficult for the Canadian labour force to enjoy full employment. The Economic Council of Canada, in its annual reviews of the Canadian economy, has stressed that an extraordinarily large expansion in total employment will be required in future if our full-employment goal is to be achieved. Since the low-income sector of our labour force generally is the first to be affected by increasing unemployment, it is in their particular interest that efforts are maintained to maximize economic growth.

The position of the Government of Alberta concerning the importance of maintaining economic growth is spelled out in "A White Paper on Human Resources Development". The following excerpts from this White Paper illustrate our position:

> "The supreme objective in developing the physical resources of a nation should be to make possible the full and free development of the human resources of that nation."

6/ Volume 3, page 12.

"Because physical resources development is absolutely essential to human resources development, the necessity of establishing and maintaining a strong provincial economy cannot be over-emphasized. The development of the physical resources of Alberta to their maximum extent must remain an explicit objective of both government and people."

" ... Human resources development is absolutely dependent on physical resources development .... While human resources development demands top priority, the cold hard fact remains that the amount of materials and finances which can be committed to this task are strictly proportional to the level of physical resources development. It is totally unrealistic to be concerned with social development, and at the same time to be unconcerned about economic development. It is totally unrealistic to make demands relative to human resources development without giving consideration to ways and means of stimulating the increases in physical resources development required to make humanitarian proposals physically possible and economically feasible."

The federal and provincial governments are allocating a substantial portion of available financial resources to education and training in order to upgrade the productivity of the Canadian work force.

The Commission's proposed taxation system, designed to achieve further redistribution of wealth, would penalize Canadians for trying to improve their lot. The proposal seems inconsistent with various government policies for improving the education and training levels of the nation's work force. Continuous upgrading should benefit all levels of government through increased productivity in the work force. There would be (i) a reduction in the relative importance of low income families and individuals - the group which the Commission identifies as "net beneficiaries"; and (ii) an increase in the relative importance of higher income groups (the better educated or trained portion of our labour force) - which is identified as "contributors". The Commission's ability-to-pay concept would increase the tax burden of the better educated and trained Canadians. In our view, therefore, this concept would act as a deterrent to Canadians improving their well-being through increased education and training.

In addition to disagreeing with this basic philosophy of the Commission as to the primary objective of the taxation system, we also disagree with the major recommendations proposed by the Commission as part of its comprehensive tax base.

2. Comprehensive Tax Base

The Commission stated that the essential features of an equitable tax structure consist of:[7/]

> "1. A comprehensive income tax base that includes virtually all changes in the taxpayer's economic power.
>
> 2. A progressive rate structure that imposes greater tax burdens, both absolute and proportionate, on those with greater comprehensive tax bases.
>
> 3. The absence of differentiation among the sources of economic power, that is, the same tax treatment for wages, business income, property income, capital gains, and gifts and bequests, without regard to the source or form of organization through which these increases in economic power flow.
>
> 4. Recognition of the family as the basic tax unit, with appropriate tax modifications to take into account variations in the particular circumstances of the unit."

The Commission defined the comprehensive tax base "as the sum of the market value of goods and services consumed or given away in the taxation year by the tax unit, plus the annual change in the market value of the assets held by the unit."[8/] The tax base would include gifts and bequests received from other tax units and imputed income (the gains realized when a person uses or consumes his own personal services or his own property), the money value of gains in kind, gains and losses on an accrued rather than on a realized basis. All of the expenses reasonably incurred to earn gains (other than personal living expenses) are allowed but no personal consumption expenditure would be deductible.

The comprehensive tax base concept is a sharp departure from the traditional concept, which holds that income should be taxed but capital should not be taxed.

Because of the inclusion of all gains in economic power in the comprehensive tax base, with the unavoidable loss of investor confidence in the climate for investment capital in Canada resulting therefrom,

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7/ Volume 2, page 42.

8/ Volume 3, page 39.

the amount of private capital available for investment eventually would be reduced. Any such reduction could have serious repercussions on the economy of Alberta, which is so dependent on foreign and domestic investment capital.

As indicated in our White Paper on Human Resources Development, it is our conviction that (i) the rate at which industrial capital is generated in the Province, together with the productivity of that capital, is of utmost importance relative to economic growth, and (ii) the generation and management of industrial capital is basically the responsibility of the private sector of the economy, and ought to be achieved primarily through private earnings, savings, and investment.

The following discussion of major Commission recommendations clearly illustrates that the comprehensive tax base concept, if implemented, will act as a deterrent to foreign and domestic investment capital. The Commission apparently failed to recognize that investment capital is in short supply.

We are also concerned that the Commission did not give sufficient attention to evaluation of administrative, bookkeeping and valuation problems which would face individuals, corporations and governments if the comprehensive tax base is adopted. These problems are discussed below in connection with specific Commission recommendations.

3. Taxation of Capital Gains

The Commission recommended taxation of all capital gains, at full and progressive rates of taxation, coupled with the deductibility of most losses. The only major exclusion would be a $25,000 lifetime capital gain on sale of residential and farm properties.

> "It may have been appropriate in years past to distinguish, for tax purposes, between gains flowing from property and those resulting from the acquisition and disposition of property, but in the current business and investment environment such a distinction has little if any significance. We are convinced that the failure to tax capital gains in Canada has no basis in principle; that it has led, and will continue to lead, to uncertainty as to which gains on the disposition of property are taxable and which are not; and that it affronts all the standards of equity and neutrality which we feel should characterize a tax system."9/

9/ Volume 3, page 325.

Of particular concern to the Government of Alberta is the Commission's admission that its recommendations to tax property gains would reduce attractiveness of petroleum investments as reflected in the following quote: 10/

> "Our recommendations to tax property gains would undoubtedly make investment in some assets less attractive. For example, investments in real property and speculative mining and petroleum shares would be realtively less attractive because after-tax expected rates of return would be reduced. But we have no doubt that by inducing more new investment in other corporate shares and in new and small businesses, the rate of increase of future output in Canada would be enhanced despite these negative effects."

Because the petroleum industry is so vital to the health of the Alberta economy, we find no comfort in the latter part of the above statement. First of all, the Commission does not identify the nature of the businesses, nor does it explain how new investment would be attracted. In fact, as expressed elsewhere in this brief, it would be hard to visualize new and small businesses starting up in Alberta with total investments comparable to the $750 million currently being invested annually by the petroleum industry.

We believe that the Commission's proposals for taxing capital gains would tend to divert investment capital to dividend paying common shares of slow-growth companies or to preferred shares, and therefore investment risk capital for new and small business would not be attracted to Alberta.

The Commission seems to believe that implementation of a capital gains tax would have an adverse effect only on the wealthy segment of our population. In our opinion, such a tax would create a serious hardship for farmers, ranchers and low income salaried and wage earners who have attempted over the years to build an estate through home ownership and other investments to be used for financial support upon retirement. This hardship will be created if the Commission's proposals are implemented because the Commission does not make provision for recognition of declines in purchasing power brought about by inflation. The Commission feels that the tax system should be based on current and not constant dollars. In support of this position the Commission stated that:

> " ... we cannot overlook the fact that there are many members of society with fixed incomes who suffer losses in economic power because of inflation and are unable to protect themselves against it." 11/

10/ Volume 3, page 341.

11/ Volume 3, page 349.

The obvious way for people on fixed incomes to hedge against inflation is to become homeowners and to invest in common stocks. Implementation of a capital gains tax would act as a deterrent to such investments. The taxpayer who invests a portion of his income, makes a greater contribution to economic growth than the taxpayer who lives up to his income, and in our opinion the former should not be penalized for saving.

A capital gains tax would be particularly onerous for farmers and ranchers, who must continually expand acreage holdings in order to increase productivity through further mechanization of operations in order to combat increasing costs. A capital gains tax would act as a deterrent to such increased size of economic farm and ranch operations and would make it more difficult for farmers and ranchers to plan for retirement. The Governments of Canada and Alberta recognize the need to develop farm units of a size which are economic and make loans to farmers to enable them to increase their capital holdings.

Regardless of whether capital gains taxes are levied on the wealthy or others, if gains are not in excess of the decline in purchasing power of money, any tax levy is a confiscation of a part of the original capital.

The Commission suggested that a number of features of its proposed tax system would "offset" taxation of capital gains. These factors included (i) reduction of top personal income tax rates from 80% to 50%, (ii) liberal loss deduction provisions, (iii) five year averaging of income for tax purposes, (iv) provision to pay amounts of income into a non interest bearing income adjustment account on a deductible basis (whereby excessive amounts of income in one year can be paid in and freed of immediate tax: then the amounts are included in income in other years as withdrawn when the general income level is lower); (v) full credit for Canadian corporation taxes; and (vi) more efficient incentives for new and small businesses.

These features may not completely offset taxation of capital gains. Further, future governments might increase tax rates above the Commission's proposed maximum rate. Regarding the loss write-off provisions, investors are not motivated by the ability to mitigate losses; they are motivated by the prospect of realizing profits.

Under the Commission's taxation system, property would be "deemed" to be realized on the death of the owner or on his leaving the country. Such a proposal is impractical and unfair, because of serious cash problems which it could cause for a property owner or his estate.

Implementation of a capital gains tax would require all taxpayers to keep detailed records of transactions throughout their complete life. Government agencies probably would not be able to keep up with valuations of capital gains. For these reasons, we cannot accept the Commission's position that to bring property gains and losses into the tax base "should not unduly increase the administrative difficulties of the tax system and, in fact .... should substantially ease administration in the long-run".12/

In countries where a capital gains tax is part of the overall taxation system, this tax makes up a very small portion of total government revenues. In view of the relative insignificance of capital gains tax as a revenue producer, it would seem imprudent to introduce a capital gains tax in Canada which is chronically short of investment capital, particularly since governments are endeavouring to encourage Canadians to invest risk capital in the development of our natural resources. As pointed out in our White Paper; "Canada is a relatively young nation; and Alberta is definitely a young Province. In many respects, Canada, and its Western provinces in particular, are still in a "period of emergence". The proposed capital gains tax would work against our ultimate objective of "Every Albertan A Shareholder". As pointed out in the White Paper:

> "With the tendency of automation to give "capital" an ever increasing role in the production of goods and services, it is desirable to do everything possible to increase the number of Albertans holding equity stock in local and national industry and receiving investment income to augment occupational income."

The Commission stated that "in the United States the taxation of property gains has had very little effect on the level of investment".13/ In our opinion, it is erroneous to compare the economy of the United States with the Canadian economy in attempting to assess the validity of incorporating a capital gains tax in Canada. The Canadian economy, particularly that of

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12/ Volume 3, page 382.

13/ Volume 3, page 339.

Western Canada, is nowhere near the level of maturity of the U.S. economy. At its present stage of development, Canada must continue to offer incentives to encourage Canadian risk capital to invest in development of our physical resources.

4. Gifts and Bequests

The Commission recommended that all gifts be taxed at full progressive rates. Any gifts or bequests received from outside the family unit would be taxable to the recipient, subject to a lifetime exemption of $5,000. Separate annual exemptions would be permitted up to $250 for individuals, up to $250 each for spouses who are members of a family unit and up to $100 for dependent children. Gifts and bequests would be eligible for the income averaging provision.

Property owned by children leaving the family unit would be taken into income of their new unit and would be taxable to them at that time.

Many of the disadvantages of taxation of capital gains are equally applicable to taxation of gifts and bequests. For example, similar bookkeeping and valuation problems would be encountered. Also, because of long-range inflationary trends, the absolute dollar value of the lifetime and annual exemptions, outlined above, are too restrictive.

Under the Commission's recommendations gifts and bequests would be subject to double taxation. Recipients would pay taxes on the fair market value of the gift or bequest and the donor would be deemed to have disposed of the property at its fair market value. Any accrued property gain would be deemed to be realized and would become taxable to the donor. It is unreasonable to expect that there should be any existence of double taxation, the very aspect which we are endeavouring to eliminate in our present system.

The combination of taxation of capital gains and gifts and bequests could lead to the forced sale of many family-owned Canadian companies or farms upon the death of the surviving parent. In such cases, 50 per cent or more of the total value of the estate could be payable as capital gains and bequest tax to the government under the Commission's proposals.

The proposal to tax gifts and bequests would result in repeal of existing estate and gift taxes which would nullify The Estate Tax Rebate Act. This Act was passed at the 1967 session of the Alberta Legislature at which time Alberta became the first and only province in Canada to make provision for the return to the estate of deceased persons, who were bonafide residents of Alberta, the entire portion of the province's share of the federal estate taxes. The Act was established as a means to remove barriers and hindrances to the generation of industrial capital in Alberta.

The Estate Tax Rebate Act makes Alberta attractive to many corporations and individuals and encourages investment in Alberta's industrial and economic development. The Act is designed to provide all Albertans with the opportunity to develop pools of private capital. We find this concept much more sensible than the Commission's proposal for taxation of gifts and bequests which would result in redistribution and dilution of capital pools.

5. Integration

The Commission's proposed system of integration of personal and corporate income taxes provides the means of passing to the shareholder the corporate income as well as the credit for the taxes paid by the corporation. The resident shareholder would be taxed on this income at full progressive rates and allowed the related credit for corporation taxes paid. Since the corporation income tax rate would equal the proposed maximum personal tax rate, the credit received by the individual for corporation taxes in many cases would exceed the personal tax payable on the corporation source income included in the personal return.

The following are the basic features of the fully integrated system recommended:[14/]

"1. The income of Canadian corporations should be subject to a flat rate of tax of approximately 50 per cent.

2. Individuals and families should be subject to progressive rates of tax with a top marginal rate of 50 per cent.

14/ Volume 4, page 7.

3. The tax base of the resident shareholder should include the corporate income paid or allocated to him, "grossed up" for the corporation tax paid.

4. The resident shareholder should receive credit against his personal income tax liabilities for the full amount of the corporation tax paid in respect of the after-tax corporate income paid or allocated to him, with a refund if the credit exceeded the liability.

5. Realized gains or losses on corporate shares should be included in income and taxed at full progressive rates.

6. The corporation should be allowed to allocate after-tax corporate income to shareholders without having to pay cash dividends.

7. The cost basis of shares should be increased when the corporation allocated retained corporate earnings to shareholders, so that share gains resulting from the retention of earnings that had been taxed to the shareholder would not be taxed again to the shareholder when realized."

Integration would eliminate the existing burden of taxing the shareholder at the corporate level on corporation profits and then taxing him again on any distribution of profits in the form of dividends. Integration would also eliminate certain "loopholes" in the present Income Tax Act, such as surplus stripping, and dual corporation tax rates. However, this latter problem could be resolved by enforcement of the present law or by introducing amendments to the existing Income Tax Act.

We are concerned that implementation of the integration proposal will create additional problems which could far outweigh the advantages. The integration proposal will create "windfall" benefits to certain stockholders and "windfall" losses to others as a result of relative changes in asset values. Resident shareholders would receive full credit for taxes paid by the company. As a result many shareholders would get refunds. No personal tax would be payable unless shares were sold at a profit. Shareholders of fixed interest securities would probably face a reduction in capital values.

Since the tax position of non-resident shareholders would remain the same, non-resident investors might be discouraged from investing in Canadian securities because of the discriminatory tax position. Financing of Alberta's resource and industrial development has depended largely on foreign investment. We are not in favour of any proposed taxation system which would reduce the availability of such investment capital.

As reflected in our White Paper, "the knowledge and capital of people from other parts of Canada and from other countries are most welcome in Alberta so long as such knowledge and capital are applied to the development of Alberta in a manner consistent with the best interests and rights of the residents of this province."

The Commission's proposals would have the tendency to shift capital investment into securities and businesses which have a history of relatively high earnings and away from "high-risk" securities where growth prospects are in lieu of current earnings. Because the resource industries of Alberta fall into the latter category we are concerned that long-range financing of these industries would be adversely affected by the Commission's integration proposals.

Implementation of the integration proposals would adversely affect both the cost and the availability of borrowed funds. Because integration would encourage investment in common shares of mature or slow growing companies, fixed-interest funds would become less attractive. Thus financing via fixed-interest securities would become more costly.[15/]

Perhaps the most serious side effect of implementation of the integration proposal would be the need for governments to finance losses of tax revenues for an indeterminate period.

The Commission recognized that implementation of integration

> " ... would result in an initial loss of tax revenues that would only be offset after a number of years by the other measures that we propose". 16/
>
> "Over the long run the full taxation of share gains would provide much of the necessary increase in revenue. The removal of most of the special industry and business tax concessions would more than make up the balance". 17/

The Commission touched briefly on several alternatives for solving this problem. These alternatives included a transitional tax on shareholders, a temporary tax on corporate source income or a once-and-for-all flat-rate tax on all existing surplus. The Commission did not seem to give the consinderation this serious problem warranted.

15/ The cost of debt securities placed in foreign countries could increase by as much as 1% because of the Commission's proposal to increase the withholding tax from 15% to 30%.

16/ Volume 4, page 77.

17/ Volume 4, page 78.

The adoption of the integration proposals will result in a great many administrative problems for corporations, shareholders and administrators of the Income Tax Act.

Corporations initially will have to report to their shareholders the basis on which the shareholders should handle the change in net worth of the corporation. In many instances corporations will not be able to provide this information to shareholders before the shareholder has to file his annual income tax return. Particularly in the case of those corporations who have investments in other corporations or who have income arising from foreign operations, it may take well over a year before they would have sufficient information to advise the shareholders. In the meantime the shareholder may have disposed of his shares. The Commission appears to have completely ignored situations where an investor may acquire shares at any given moment during the year and then sell them before the end of the corporation's fiscal year. The investor who happens to own some shares in foreign securities might well have trouble obtaining the information from the foreign company in order to properly file his tax return. A great many shareholders have little or no bookkeeping experience and the rules and regulations which they will face may be sufficient to deter many of them from making such investments.

Under the present regulations those responsible for federal government policies can change corporate rates and personal income tax rates independently in order to assist in directing the economy of the country as a whole. Once corporate and personal income taxes are integrated the use of this device will be greatly restricted. The overall benefits to be gained by integration do not appear to outweigh the loss of the use of this tool. If a future federal government were to try to use this tool it would probably be on a basis of partially withdrawing from full integration. It would always be possible to impose a corporation tax which could not be claimed by the individual shareholder when filing his return or, on the other hand, it would be possible to state that the individual shareholder can only claim a percentage of the corporation tax. When either of these moves are made the integration theory of the Commission collapses. Some provincial governments are charging a higher rate of corporation tax than others. Since the Commission made a plea for full

co-operation between provinces and federal taxing authorities, we must presume that the Commission anticipates that this situation will be changed and no longer operative. This assumption does not appear to be based on fact.

6. Single Package Concept

The Commission by its own admission has recommended many fundamental changes which, if adopted, would produce a complete transformation. Despite the revolutionary nature of its proposed tax system, the Commission stated:

> "It is essential in evaluating the effects of our proposed tax reforms, that they be considered as a package rather than piecemeal". 18/

The package concept of the Report is unrealistic for a number of reasons. For example, the Commission proposes to replace the existing Income Tax Act, which though imperfect has survived the test of time, with a theoretical untested taxation system as a single package. The present Income Tax Act has the force of time and jurisprudence behind it whereas the integration proposals are fraught with the unknown and are bound to be replete with many new problems which will have to be solved over the next number of years before taxpayers, their advisors and the governmental officials involved will be able to understand the new law completely.

Further, the Commission seemed to assume that future governments would be bound by the proposed package if implemented. In actual fact, there would be nothing to prevent future governments from changing various, if not many, aspects of the Commission package. Such changes would disturb the relationship between individual components of the proposed system. For example, future governments could increase the maximum tax rates above 50 per cent.

As pointed out elsewhere in this Chapter, the Commission seems to have underestimated the administrative, bookkeeping and valuation procedures which will be necessary for taxpayers and government under its proposed taxation system. In discussing integration and the full taxation

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18/ Volume 2, page 48.

of capital gains, the Commission states:[19/]

> "We believe that the greater the initial step and the fewer the subsequent steps, the less would be the total market disturbance."
>
> " ... A single step making the full change would probably be no more disturbing if accompanied by all the other reforms we have proposed."

For reasons outlined above, we are unable to accept these opinions.

The Commission should have been able to anticipate that not all aspects of its package concept would be acceptable to taxpayers or government. Inequities, loopholes, obsolete or unattractive features of our present Act could have been corrected without resorting to a completely revolutionary, untested income taxation system. It seems unwise to enact an entirely new system at this point when the results from an economic standpoint are so uncertain.

The package concept has definite and serious inherent weaknesses, a few of which were outlined above. For these reasons we believe the single package concept proposed by the Commission should be rejcted. Further, the major tax reforms included in the package are also equally unattractive to the Government of Alberta as individual tax reforms.

Brief reference will now be made to the other major recommendations of the Commission.

7. Deferred Income: Retirement Plans and Pension Plans

The Commission has proposed that instead of having certain limitations on the annual amounts which can be contributed to various registered plans, the only limitation should be based on the eventual benefits which can be taken out of the plan at age 65 years on an annuity basis. They have suggested a maximum annuity of $12,000 covering both husband and wife, with a maximum guaranteed term of 10 years; if, however, the wife is more than 10 years younger than the husband, for purposes of their provisions, her age would be deemed to be only 10 years younger.

19/ Volume 4, page 75.

There appears to be merit in the effort to obtain a uniform tax treatment of pension and other retirement savings plans. Also there appears to be merit in eliminating the ceilings on the permissable annual deductions.

We believe that these apparent benefits must be very carefully weighed against other problems which will result from the Commission's recommendations. With even limited inflation this figure may be comparatively low for a person entering the labour force today, particularly if he has a university degree.

8. Single Rate of Corporation Tax

Under the proposed single tax rate, problems resulting from the present dual rate would disappear, such as associated companies, distinguishing income and capital, etcetera.

The Commission recognized that the proposal could create a hardship for new and small business. The Commission hopes to alleviate such a disadvantage by providing accelerated 100 per cent capital cost allowances. New and small businesses would be those with assets under $1 million and at least 70 per cent controlled by Canadian residents. The upper limit of assets that could be written off immediately would be $250,000.

The Commission's proposal does not take into account the problem created for many small service companies which do not have fixed assets to be written off rapidly and yet who would be penalized by the shift from a 21 per cent rate to a 50 per cent tax rate. Further, the Commission's proposal does not prove that, even for many companies with investment in fixed assets the accelerated capital cost allowance would offset the increase to a 50 per cent tax rate.

9. Income of Canadian Corporations from Outside Canada

The Commission's proposal would make foreign investments by Canadians less attractive.

This recommendation could be disturbing for Canadian companies which presently have or plan to have foreign operations.

Canadian companies considering investment abroad would have to be able to foresee much higher returns from such investments outside Canada since Canadian shareholders would not enjoy full integration of such earnings. For this reason, and because of the proposed minimum rate of taxation of income earned abroad Canadian companies would be disinclined to make such investments. Several sizeable Alberta companies have expanded their operations to a worldwide level. Their contribution to both the Alberta and Canadian economy is well recognized. It would be regrettable to discourage their further expansion or expansion of other domestic companies into the international field.

10. Summary

In our opinion a tax system structured to maximize economic growth would be preferable to one designed to provide equity and redistribution of wealth as proposed by the Commission. A system designed to maximize economic growth in the long-run would be of greater value to all income groups, and would be consistent with educational and training policies of various levels of government.

The proposed taxation of capital gains is inappropriate in the case of a relatively young nation like Canada which is in the "period of emergence" and needs to provide incentives to investors to place their savings in natural resource investments. Taxation of capital gains would create a hardship for all Canadians who are endeavouring to invest their savings in home-ownership and other investments. It would be particularly harmful for Canadian farmers and ranchers. Proposed taxation of gifts and bequests would create similar problems.

The proposal for integration of personal and corporate income taxes would create a number of problems including greater centralization of fiscal power in the Federal Government, the need to find additional revenue sources to offset short-term and long-term reductions in tax revenues, serious administrative, bookkeeping and valuation problems for taxpayers, businesses and government, and the probability of increasing the cost of fixed income borrowing so necessary in government financing.

The single package concept deemed by the Commission is both unrealistic and unnecessary. Many of the problems of the existing Act could be eliminated without creating an entirely new Act untested by time and jurisprudence.

Other major recommendations of the Commission are not as onerous but could create administrative, bookkeeping and valuation problems for those concerned.

Appendix Table A

SALIENT STATISTICS ABOUT ALBERTA'S NATURAL RESOURCES AND ECONOMIC DEVELOPMENT

Agriculture

	Improved Land		Unimproved Land		Total Farm Area	
	Acres (000's)	Per Cent of Total Canada	Acres (000's)	Per Cent of Total Canada	Acres (000's)	Per Cent of Total Canada
Alberta	25,288	24.5%	21,940	31.7%	47,229	27.3%
Saskatchewan	43,117	41.6	21,297	30.8	64,416	37.4
Manitoba	11,964	11.6	6,205	9.0	18,170	10.5
Total Canada	103,403	100.0%	69,147	100.0%	172,551	100.0%

Source: 1966 Canada Year Book, page 511, 1961 data.

	Manitoba	Saskatchewan	Alberta (thousand head)	Canada	Alberta to Canada (%)
Horses	39	84	96	424	23%
Cattle (beef)	957	2,107	2,861	9,912	29
Cattle (dairy)	182	193	274	2,906	9
Swine	450	505	1,370	5,620	26
Sheep	66	165	409	1,287	32

Source: 1966 Canada Year Book, page 487, 1964 data.

	Alberta	Saskatchewan (millions of dollars)	Total Canada	Alberta to Canada (%)
Wheat	$258	$863	$1,259	20%
Oats	66	65	281	24
Barley	111	74	208	53
Tame Hay	61	25	377	16

Source: 1966 Canada Year Book, page 481ff, 1963 data.

Forestry

	Unit	Alberta	Canada	Alberta to Canada
Suitable for saw timber	(millions of cubic feet)	25,584	479,165	5.3%
Suitable for pulp	(millions of cords)	346	3,208	10.8%

Source: Western Canada - Land of Resources.

Economic Development - Employment and Labour Force

	1946	1951	1961	1966	1946	1951	1961	1966
	(thousands)				(per cent)			
Agriculture	121.5	115.0	103.6	94.0	40.3	32.5	21.1	16.8
Services	64.1	71.8	132.0	185.0	21.2	20.2	27.0	32.9
Wholesale & Retail Trade	30.1	46.8	80.1	88.0	9.9	13.2	16.4	15.7
Manufacturing	27.9	35.6	42.2	51.4	9.2	10.1	8.6	9.2
Transportation, Storage, Communication, Electric Power, Gas & Other Utilities	23.1	30.3	47.4	53.6	7.6	18.6	9.7	9.6
Construction	12.9	25.7	37.4	43.5	4.3	7.3	7.6	7.8
Mining & Oil Wells	10.3	15.7	17.4	18.9	3.4	4.4	3.6	3.4
Finance, Insurance & Real Estate	5.0	8.0	14.7	15.7	1.6	2.3	3.0	2.8
Others	7.7	5.0	14.7	9.9	2.5	1.4	3.0	1.8
	302.6	353.9	489.5	560.0	100.0	100.0	100.0	100.0

Source: Government of the Province of Alberta.

Appendix Table B

PROBABLE REMAINING PETROLEUM INDUSTRY RESERVES - YEAR END 1966

Alberta and Canada

PRODUCT	UNIT	ALBERTA	TOTAL CANADA	ALBERTA % OF TOTAL
Crude Oil	Billion Barrels	8.4	9.8	85.7
Natural Gas Liquids	Billion Barrels	1.4	1.5	93.3
Total Liquid Hydrocarbons	Billion Barrels	9.8	11.3	86.7
Natural Gas	Trillion Cubic Feet	39.7	49.3	80.5
Elemental Sulphur	Million Long Tons	99.7	102.8	97.0

Source: Canadian Petroleum Association, Statistical Year Book 1966.

Appendix Table C

NET VALUE OF GENERAL INDUSTRY PRODUCTION

Alberta

	Selected Years									
	1946		1951		1956		1961		1966	
INDUSTRY - ALBERTA	Millions of Dollars	%	Millions of Dollars	%	Millions of Dollars	%	Millions of Dollars	%	Millions of Dollars	%
Agriculture	309.1	58.7	505.8	49.8	402.2	26.4	368.8	21.2	630.2	23.1
Forestry	8.6	1.6	10.2	1.0	14.7	1.0	17.3	1.0	12.0	0.8
Fisheries	10.6	0.1	0.5	-	0.8	0.1	0.9	0.1	0.8	-
Trapping	3.0	0.6	2.5	0.2	1.1	0.1	1.7	0.1	1.8	0.1
Mining	47.6	9.0	151.6	14.9	380.8	25.0	460.2	26.5	850.0	31.2
Electric Power	9.0	1.7	16.6	1.6	32.8	2.2	52.6	3.0	75.0	2.8
Manufacturing	83.7	15.9	141.6	13.9	285.8	18.7	346.4	19.9	500.0	18.4
Construction	64.6	12.3	187.4	18.4	406.1	26.6	490.7	28.2	643.1	23.6
TOTAL	526.2	100.0	1,016.2	100.0	1,524.3	100.0	1,738.6	100.0	2,722.8	100.0

Source: Dominion Bureau of Statistics - SURVEY OF PRODUCTION.

Note: Totals may not add due to rounding. Different years are not strictly comparable. Changes ocurred in the manufacturing and mining categories in 1959 and 1961, and in the electric power category in 1956.

Appendix Table D

NET VALUE OF PRODUCTION IN MANUFACTURING INDUSTRIES

Alberta

INDUSTRY	Selected Years							
	1951		1956		1961		1965	
	($ MM)	%	($ MM)	%	($ MM)	%	($ MM)	%
Food & Beverage	54.9	38.8	83.1	29.1	95.2	27.4	132.7	27.8
Clothing, Textiles, Knitting & Leather	3.6	2.5	6.5	2.3	10.2	2.9	15.4	3.2
Wood, Paper, Furniture & Fixture, Printing & Publishing	31.3	22.1	47.3	16.6	64.9	18.7	91.4	19.2
Primary Metal					21.4	6.2	28.3	5.9
Machinery, Electrical Products & Transportation Equipment	20.9	14.8	49.6	17.4	17.7	5.1	23.3	5.0
Other Metal Fabricating					26.3	7.6	44.9	9.4
Non-Metallic Mineral Products	11.0	7.8	21.5	7.5	34.9	10.1	46.2	9.7
Petroleum & Coal Products	12.1	8.5	52.0	18.2	30.1	8.7	30.9	6.5
Chemicals & Chemical Products	6.3	4.4	23.2	8.1	33.8	9.7	50.2	10.5
Other	1.5	1.1	2.6	0.9	12.2	3.5	13.0	2.7
TOTAL	141.6	100.0	285.8	100.0	346.7	100.0	476.4	100.0

Note: Totals may not add due to rounding. Classification changes means that figures shown may not be strictly comparable. However, the principal change appears to be in the petroleum category: absorption plants were transported from the mining sector.

Sources: Dominion Bureau of Statistics - MANUFACTURING INDUSTRIES OF CANADA, Section E.
Alberta Bureau of Statistics - ALBERTA INDUSTRY AND RESOURCES - 1964.

Appendix Table E

VALUE OF MINERAL PRODUCTION

Province of Alberta

(millions of dollars)

Year	Crude Oil	Natural Gas	Sulphur	Total Crude Oil, Natural Gas & Sulphur	Total Mineral Production	Crude Oil, Natural Gas & Sulphur - % of Total Mineral Production
1946						
1947				21.5	60.1	36%
1948				43.4	93.2	47
1949				61.6	113.7	54
1950				85.1	135.8	63
1951	113.9	3.5		117.4	168.1	70
1952	139.5	5.9		145.4	196.8	74
1953	193.8	6.7		200.5	248.9	80
1954	228.3	8.0		236.3	279.0	85
1955	274.9	10.0		284.9	326.0	88
1956	353.6	11.0		364.6	411.7	89
1957	355.6	13.7		369.3	410.2	90
1958	283.3	20.1	1.6	305.0	345.9	88
1959	306.9	25.0	1.6	333.5	376.2	89
1960	302.8	34.1	3.3	340.2	395.3	86
1961	355.5	48.9	5.7	410.1	473.0	87
1962	379.8	88.7	7.5	476.0	567.0	84
1963	416.8	129.4	11.2	557.4	669.0	83
1964	450.2	149.6	14.6	614.4	747.0	82
1965	474.3	169.4	16.7	650.4*		
1966	524.0	180.0	16.6	720.6*		

Source: CANADA YEAR BOOK - 1966
FINANCIAL POST SURVEY OF OIL - various years.

* Estimated.

Appendix Table F

VALUE OF MINERAL PRODUCTION

Alberta and Canada

Year	Alberta	Canada	Alberta % of Canada
	(millions of $)		
1946	60	503	11.9
1947	67	645	11.4
1948	93	820	11.3
1949	114	901	12.7
1950	136	1045	13.0
1951	168	1245	13.5
1952	197	1285	15.3
1953	249	1336	18.6
1954	279	1488	18.8
1955	326	1795	18.2
1956	411	2084	19.7
1957	410	2190	18.7
1958	346	2101	16.5
1959	376	2409	15.6
1960	395	2493	15.9
1961	473	2582	18.3
1962	567	2851	19.9
1963	669	3050	22.0
1964	747	3397	22.0

Source: CANADA YEAR BOOK - 1959 & 1966.

Appendix Table G

GROSS VALUE OF CONSTRUCTION (New and Repair)

Alberta

TYPE OF CONSTRUCTION	Selected Years: 1953 Total ($ MM)	1953 Total (%)	1956 Total ($ MM)	1956 Total (%)	1961 Total ($ MM)	1961 Total (%)	1966 Total ($ MM)	1966 Total (%)
Building Construction								
Residential	123.0	22.1	155.6	21.4	195.3	22.3	209.7	17.3
Industrial	27.4	4.9	37.3	5.1	13.8	1.6	18.6	1.5
Commercial	55.5	10.0	60.8	8.4	63.7	7.3	120.1	9.9
Institutional	30.9	5.6	42.0	5.8	60.6	6.9	163.4	13.5
Other:	45.4	8.2	49.6	6.8	56.8	6.5	15.1	1.3
(Farm Buildings 1/)	(22.8) 1/	(4.1) 1/	(25.6) 1/	(3.5) 1/	(40.8) 1/	(4.7) 1/	(38.4) 1/	(3.2) 1/
TOTAL	282.1	50.7	345.4	47.6	390.2	44.5	526.9	43.5
Engineering Construction								
Roads, Highways & Aerodromes	65.3	11.7	74.1	10.2	101.1	11.5	87.7	7.2
Waterworks & Sewage	19.7	3.5	28.7	4.0	16.6	1.9	32.0	2.6
Electric Power	12.1	2.2	21.5	3.0	20.8	2.4	21.0	1.7
Railway, Telephone & Telegraph	26.6	4.8	30.0	4.1	32.3	3.7	53.1	4.4
Gas & Oil Facilities:	115.5	20.8	199.6	27.5	282.8	32.3	346.8	28.6
Oilwells	68.3	12.3	133.3	18.4	89.3	10.2	177.9	14.7
Gas Wells	10.9	2.0	7.8	1.1	37.1	4.2	60.2	5.0
Oil Pipelines	17.5	3.1	15.8	2.2	14.3	1.6	57.0	4.7
Gas Pipelines	3.8	0.7	6.1	0.8	60.1	6.9	4.5	0.4
Pumping Stations	4.0	0.7	4.3	0.6	2.4	0.3	9.2	0.8
Storage Tanks	4.2	0.8	5.9	0.8	4.4	0.5	0.7	0.1
Oil Refining - Processing Units	2.7	0.5	10.0	1.4	3.6	0.4	3.9	0.3
Natural Gas Cleaning Plants	1.0	0.2	10.5	1.4	67.3	7.7	26.5	2.2
Gas Mains and Services	3.2	0.6	5.8	0.8	4.1	0.5	7.0	0.6
Other	34.8	6.3	26.3	3.6	32.9	3.8	143.7	11.9
TOTAL	274.0	49.3	380.2	52.4	486.5	55.5	684.4	56.4
TOTAL VALUE OF CONSTRUCTION	556.0		725.6		876.7		1,211.3	

Note: Totals may not add due to rounding.

1/ Excludes dwellings.
(Figures in brackets are not additive.)

Source: Dominion Bureau of Statistics, Construction in Canada.

Appendix Table H

NET GENERAL REVENUE[1/]

Provincial Government of Alberta

	Selected Years									
	1946		1951		1956		1961		1967[8/]	
TYPE OF REVENUE	($ MM)	%	($ MM)	%	($ MM)	%	($ MM)	%	($ MM)	%
Taxes on Income:										
Personal	*	-	*	-	-	-	-	-	76.6	15.2
Corporate	-	-	4.3	4.1	-	-	-	-	33.0	6.6
Total	-	-	4.3	4.1	-	-	-	-	109.6	21.8
Taxes on Consumption:										
Amusements etc.2/	n.a.		1.0	0.9	1.4	0.6	0.9	0.3	1.3	0.2
Gasoline and Fuel	n.a.		13.1	12.4	22.8	9.4	33.8	12.4	51.2	10.6
Total	5.8	14.1	14.1	13.3	24.2	10.0	34.7	12.7	52.5	10.4
Taxes on Assets:										
Business 4/, 6/	2.1	5.1	1.0	0.9	*	-	2.1	0.8	3.8	0.7
Estate (or Succession)	0.9	2.2	-	-	-	-	-	-	5.0	1.0
Total	3.0	7.3	1.0	0.9	-	-	2.1	0.8	8.8	1.7
TOTAL TAXES	8.8	21.4	19.4	18.3	24.2	10.0	36.9	13.5	170.9	33.9
Privileges, Licences and Permits[3/]	8.4[6/]	20.4	14.3	13.5	21.7	9.0	26.4	9.7	37.8	7.5
Petroleum and Natural Gas Revenues:										
Crown Reserve Sales	n.a.		13.2	12.5	69.1	28.6	44.3	16.2	110.0	21.9
Royalties	n.a		11.0	10.4	37.3	15.5	39.2	14.4	76.0	15.1
Fees and Rentals	n.a.		15.4	14.6	25.8	10.7	32.4	11.9	52.0	10.3
Total	n.a.		39.6	37.4	132.2	54.8	115.9	42.5	238.0	47.3
Government of Canada:										
Tax Rental and Sharing[5/]	5.8	14.1	14.8	14.0	37.3	15.5	58.4	21.4	3.5	0.7
Subsidies5/	5.1	12.4	2.9	2.7	4.0	1.7	4.6	1.7	2.9	0.6
Total	10.9	26.5	17.7	16.7	41.3	17.1	63.0	23.1	6.4	1.3
Other Revenue[7/]	13.1	31.8	14.8	14.0	21.9	9.1	30.8	11.3	50.2	10.0
TOTAL NET GENERAL REVENUE	41.2		105.8		241.3		273.0		503.3	100.0

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Note: Totals may not add due to rounding.

* Less than $50,000.

1/ Fiscal year ended nearest December 31.
2/ Includes amusements and admissions.
3/ Excludes petroleum and natural gas industry.
4/ Includes fire prevention tax.
5/ Rebates on public utility tax included with subsidies.
6/ Includes some petroleum industry payments.
7/ Includes profits from government-operated Alberta Liquor Control Board.
8/ Figures in this year are estimates only.

Sources: Dominion Bureau of Statistics, Financial Statistics of Provincial Governments; Province of Alberta.
E.J. Hanson, Fiscal Needs of the Canadian Provinces (1964).

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